



S500

9-11-07

**JERRY SANDERS**  
MAYOR

September 4, 2007

Mr. Kelly C. Bowers  
Senior Assistant Regional Director  
Securities and Exchange Commission  
Los Angeles Regional Office  
5670 Wilshire Boulevard, 11<sup>th</sup> Floor  
Los Angeles, CA 90036-3648

Dear Mr. Bowers:

This is in response to your July 23, 2007 letter to Messrs. John Hartigan and Stanley Keller regarding Mr. Keller's "Initial Report of Independent Consultant" dated June 7, 2007.

Let me first assure the Securities and Exchange Commission (SEC) that I take the need to reform City government very seriously and this has been a top priority of mine ever since taking office nearly 20 months ago. To this end, there have been a number of initiatives I have already taken forward and that have been approved by the City Council. Many more are underway and will be brought forward as they are completed. Attachments 1 through 5 discuss the City's progress on implementing the recommendations found in the "Report of the Audit Committee" (Kroll Report) dated August 8, 2006.

Speaking specifically to the recommendations in Mr. Keller's report and noted in your letter:

1. **The City must finalize the internal audit function and hire as soon as possible a qualified internal auditor.**

The City concurs with this recommendation and is in the final stages of filling the internal auditor position. Interviews of seven finalists were held on July 26, 2007 and the top two candidates have been interviewed. A final decision and offer will be made shortly and an announcement made once an agreement for employment is reached. In the meantime, in May of this year I appointed a well-qualified Interim Internal Auditor who has re-activated the Internal Audit Unit, including the development of a City-wide risk assessment.

2. **The Audit Committee should complete its organization as quickly as possible by selecting citizen advisers and professional consultants, as necessary, to assist the Audit Committee in discharging its responsibilities.**

While Kroll recommended the establishment of an Audit Committee comprised of two "public" members and one City Council Member, the City Attorney has opined that this structure of an Audit Committee could not be implemented without a change to the City's Charter. As such, the City Council established an Audit Committee comprised of three City Council Members.

Attachments 6 through 8 are the charter, ordinance establishing the Audit Committee, and statement of operating principles relating to the Audit Committee and its relationship with the Internal Auditor. In addition to the three City Council voting members, there are three ad hoc advisers confirmed at the July 30, 2007 Audit Committee meeting who will bring technical expertise to the Committee. The Audit Committee is also in the process of retaining a consultant with professional auditing and accounting expertise to assist the Audit Committee perform its oversight function.

On a parallel track, I established a 15 member City Charter Review Committee comprised of one member nominated by each Council Member and seven appointed by me. The charge of the Committee is to review a number of Charter related issues and ultimately submit recommended Charter amendments to the City Council. This is to be completed by September 2007 for consideration for inclusion on the June 2008 ballot. One of the items being discussed is to amend the Charter to establish a permanent Audit Committee, as well as suggesting the permanent make-up of the Committee.

3. **The City should upgrade to a more modern and reliable financial accounting system so as to ultimately improve financial reporting.**

The City concurs with this recommendation and has already selected a new software vendor. The current schedule calls for the implementation of a new core financial system by July 2008 and the human resources/payroll system by January 2009. This is moving as fast as can reasonably be expected.

4. **The City should re-evaluate the role and accountability of its Chief Financial Officer and consider having the same person serve as the Chief Financial Officer and Auditor and Comptroller.**

Upon taking office, I established the City's first ever Chief Financial Officer (CFO) position. As part of this action, I consolidated all financial related activities and responsibilities under this position. About one year after the establishment of this position, the City's Auditor and Comptroller left the City, providing the City with an opportunity to take those responsibilities and assign them specifically to the CFO. This is the first step in separating the internal audit responsibilities from the comptroller duties and is consistent with a recommendation made by Kroll. Again, because of an opinion by the City Attorney, this Kroll recommendation cannot be fully implemented without a Charter amendment and is also an item of discussion by the Charter Review Committee.

5. **The City should continue evaluating the disclosure process and consider whether moving toward a shelf-like disclosure system would be appropriate.**

The Independent Consultant's Report stated that "it will be desirable for the City to consider whether to move toward a more shelf-like disclosure system, similar to that used by private issuers, as a way to permit accessing the capital markets in a timely and efficient manner in order to achieve savings for taxpayers and ratepayers." The Independent Consultant made this suggestion in light of the comprehensive disclosure processes of the City's, including the Disclosure Controls and Procedures of the City's Disclosure Practices Working Group (the "DPWG") (Attachment 9). The City's current disclosure processes and procedures were enacted by Ordinance No. 0-19320 (Ordinance), adopted by the City Council on October 11, 2004. The

formation of the DPWG was in response to recommendations made by the law firm Vinson & Elkins L.L.P. in its report of September 16, 2004, regarding deficiencies in the processes and practices of the City with respect to the disclosure of financial information to the financial markets.

The DPWG is a cross-disciplinary internal working group of the City (currently composed of the City Attorney, the Chief Deputy City Attorney for Finance and Disclosure, City's Chief Financial Officer, the Debt Management Administrator, and the City's outside Disclosure Counsel, along with the City Council's Independent Budget Analyst as an ex-officio member)<sup>1</sup> designed to ensure communication between City departments, to create a clearinghouse to discuss and debate best practices with respect to disclosure controls and procedures, and to directly address the deficiencies cited in the Vinson & Elkins report. The objectives of the DPWG are twofold: to ensure the compliance of the City (and the City Council, City officers, and staff in the exercise of their official duties) with federal and state securities laws and to promote the highest standards of accuracy in disclosures relating to securities issued by the City.

The City is carefully reviewing the suggestion of the Independent Consultant, including the evaluation of so-called shelf-registration models currently in use by a limited number of public agencies that frequently access the public markets, especially if the current model is too cumbersome to ensure the timely process of documents as the City regains access to the public markets. The City has adopted improved procedures for the review of its Comprehensive Annual Financial Reports which can serve as the basis for such a shelf-registration process should it proceed in that direction. The City is mindful, however, that its current disclosure regime has made significant improvements to the City's controls regarding the release of financial information to the public capital markets. Accordingly, any shelf-registration model would take into consideration procedures currently in place which were designed to ensure that the City would not make misleading statements or omissions to the market place in the future.

In addition to the above, the City is moving forward on many fronts, including having issued its fiscal year 2003 and 2004 Comprehensive Annual Financial Reports, implementing additional Kroll remediation recommendations, working on strengthening its internal controls and filling key positions.

Sincerely,

Mayor Jerry Sanders

Enclosure: Attachments 1-9

Cc: Audit Committee/City Council  
City Attorney  
Chief Financial Officer  
Independent Budget Analyst

<sup>1</sup> The current composition of the City's Disclosure Practices Working Group reflects the evaluation by the Independent Consultant. See the memorandum of the Independent Consultant, dated April 20, 2007 entitled "Memo of the Independent Consultant on the Disclosure Practices Working Group" attached hereto as Attachment 9. The City adopted the Independent Consultant's recommendation on April 30, 2007. The City expects to adopt an ordinance implementing changes to the DPWG in September 2007.



## THE CITY OF SAN DIEGO

### OFFICE OF THE INDEPENDENT BUDGET ANALYST REPORT

**Date Issued:** August 29, 2007

**IBA Report Number:** 07-80

**City Council Docket Date:** September 4, 2007

**Item Numbers:** 332 and 333

**Item:** Background Information for Item 332 - Report from the Independent Consultant (Stanley Keller) and Item 333 - Response to the SEC

#### RECAP OF INDEPENDENT CONSULTANT/MONITOR CONTRACT

The purpose of this report is to provide background information for Council and the public with respect to two items on next week's docket that relate to the status of the City's financial reforms. The first item, Item 332, is an information report from Stanley Keller in his capacity as the City's **Independent Consultant** as required by the Securities and Exchange Commission (SEC) in their Order of November 14, 2006. The SEC required that the City retain an Independent Consultant for a period of three years to review and make recommendations regarding the City's policies and internal controls with respect to its financial disclosure functions. A three year contract with Mr. Keller was recommended by the Mayor and approved by Council on January 16, 2007.

This contract also provided for Mr. Keller to serve in the capacity of "**Monitor**" as recommended by the Kroll report that was issued on August 8, 2006. In his role as Monitor, Mr. Keller is to assist with review and implementation of remediation measures as recommended by Kroll. While there is natural overlap between Independent Consultant and Monitor duties, it is important that they be distinct in their execution. Given the crossover of issues, the intent of Mr. Keller serving in both roles was to take advantage of knowledge he has acquired about San Diego's reform efforts in order to achieve efficiencies.

#### INITIAL REPORT OF INDEPENDENT CONSULTANT TO THE CITY OF SAN DIEGO (Item 332)

The SEC Order calls for the designated Independent Consultant to issue three reports to the SEC as follows: "issue its first report within 120 days after the date of the engagement and the following two reports within 60 days following each subsequent one-year period from the date of engagement." With Mr. Keller's contract with the City

**Office of Independent Budget Analyst**

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being executed on or about January 27, 2007, his first report, using that date, was due to the SEC on May 28, 2007. However, Mr. Keller requested of the SEC, and the SEC approved, an extension to June 8, 2007. Mr. Keller indicated he requested an extension in order to allow for items that were underway to be finalized and reflected in the report. Future requests for extension should first be approved by the Mayor and City Council.

Mr. Keller issued his report to the City Council, the Mayor's Office and the City Attorney as well as to the SEC on June 7, 2007. As Mr. Keller did not present his report to the City Council upon its release, this item is docketed so that he can discuss his report in a public forum and respond to questions.

### **LETTER FROM SEC IN RESPONSE TO THE INDEPENDENT CONSULTANT'S INITIAL REPORT (Item 333)**

On Monday, July 23, 2007 Stanley Keller, Independent Consultant, and John Hartigan, the City's outside legal counsel on this matter, received a letter from Kelly C. Bowers, SEC Senior Assistant Regional Director, in response to the Independent Consultant's June 7<sup>th</sup> Initial Report. Mr. Keller provided the letter to the CFO and the City Attorney's Office the same day he received it, and he suggested that it be provided to the Chair of the Audit Committee. The correspondence was not similarly distributed to the Council President, members of the City Council or the IBA on the 23<sup>rd</sup>. It was provided to the Chair of the Audit Committee at the end of the week and to the City Council on Monday, July 30<sup>th</sup>. Timely distribution of important SEC communications is critical to both branches of government, and responsibilities for this should be clarified for the future.

The letter from the SEC requested that additional information be provided on the steps taken by the City to adopt the following items discussed in Mr. Keller's report:

- Finalizing the internal audit function and hiring a qualified internal auditor
- Completing the organization of the Audit Committee and selecting citizen advisors and professional consultants to advise them
- Upgrading to a new financial accounting system
- Reevaluating the roles and accountability of the CFO and the Auditor and Comptroller
- Evaluating the disclosure process and consider moving to a shelf-like disclosure system

The letter stated: "please advise us as soon as possible as to the steps taken by the City to adopt the above recommendations or other alternative methods designed to achieve the same objectives... We are also interested in knowing the estimated timeframe for implementing these recommendations."

Since the letter was addressed to Messrs. Keller and Hartigan, I asked Mr. Keller to clarify whether the response should come from him or directly from the City. Mr. Keller noted that the City should be responding directly "since it is the City's response to my (Mr. Keller's) recommendations." At a special Audit Committee meeting of August 6<sup>th</sup>, the CFO discussed several points that he suggested be included in a City response. It was also noted at this meeting that this item would be scheduled for full Council discussion on September 4<sup>th</sup>, 2007 - the first Council meeting following legislative recess. In a letter sent on August 7<sup>th</sup>, the CFO notified the SEC regarding this schedule. This item has been docketed in order to discuss and coordinate a City response.

The IBA believes that a coordinated response regarding steps taken and planned actions will best convey the City's commitment to be responsive to the items noted in the SEC letter of July 23<sup>rd</sup>, 2007.

This report is provided for information only.



Andrea Tevlin  
Independent Budget Analyst



THE CITY OF SAN DIEGO

August 7, 2007

Mr. Kelly C. Bowers  
Senior Assistant Regional Director  
Securities and Exchange Commission  
Los Angeles Regional Office  
5670 Wilshire Boulevard, 11<sup>th</sup> Floor  
Los Angeles, CA 90036-3648

Dear Mr. Bowers,

The City is in receipt of your July 23, 2007 letter to Messrs. John Hartigan and Stan Keller regarding Mr. Keller's "Initial Report of Independent Consultant" dated June 7, 2007 and is in the process of preparing a formal written response.

The City Council is on legislative recess for the month of August. The Mayor would like to formally meet with the Council prior to sending the City's response and has worked with the City Council President to docket the item for the September 4 Council meeting. The City's response will be sent shortly thereafter.

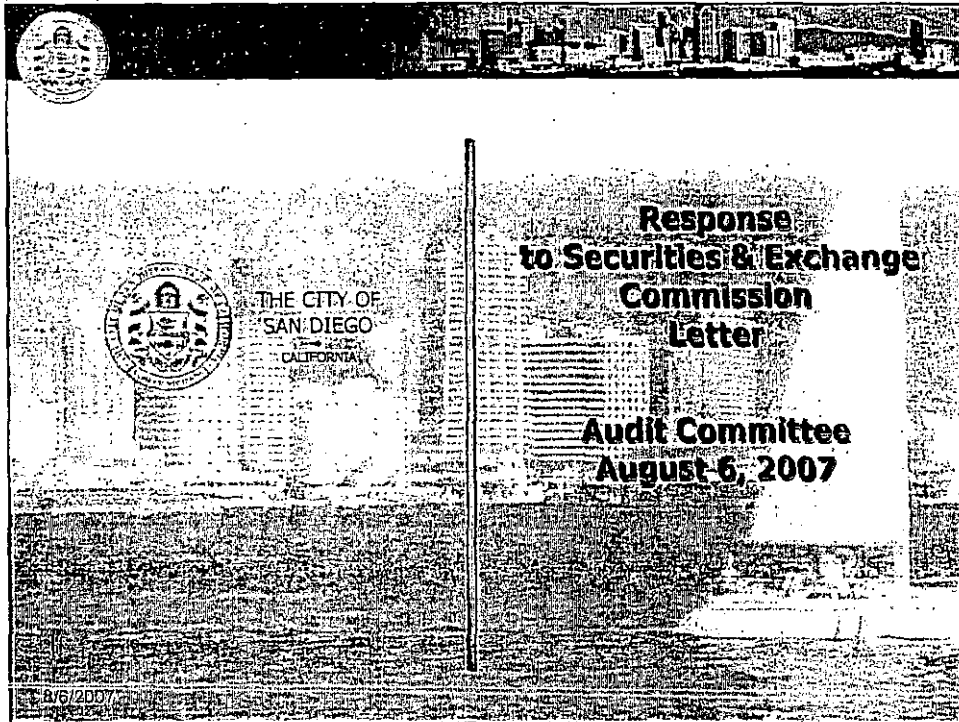
Should you have any questions in the meantime, feel free to contact me at 619-236-7080.

Thank you.

Sincerely,

Jay M. Goldstone  
Interim Chief Operating Officer/Chief Financial Officer

Cc: Jerry Sanders, Mayor  
City Council Audit Committee  
City Councilmembers  
Mike Aguirre, City Attorney  
Stan Keller, Independent Consultant  
Andrea Tevlin, Independent Budget Analyst



## Overview

- Components of the response
- Timing of response
- Audit Committee's comments/input

8/6/2007

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## The Response

- Describe work completed to date
- Provide the 6 Kroll remediation status reports
- Respond specifically to each of the 5 areas
- Acknowledge work still to be done

*possible Council response*

8/6/2007

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## Internal Auditor

- The appointment of an Interim Internal Auditor
- Development of Risk Assessment
- Recruitment process
  - 19 applications
  - July 26<sup>th</sup> – 7 candidates interviewed
  - August – Top 2 candidates to be interviewed
  - Late August – Possible offer to be made

8/6/2007

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## Audit Committee

- Acknowledge the establishment of a 3 Council Member Audit Committee
- July 30<sup>th</sup> Meeting – 3 technical experts added in an ex-officio capacity
- Apprise of work performed
- Share copy of Charter, Bi-laws and Statement of Operating Principles
- Mention work of Charter Review Committee

*RFP - professional consultant*

8/6/2007 5



## Financial Accounting System

- Council approved the acquisition of SAP
- July 2008 – Implement Core Financial System
- January 2009 – Implement Payroll/HR System

8/6/2007 6



## Role of Chief Financial Officer

- Establishment of the CFO position
- The consolidation of financial oversight
- Separation of the Internal Auditor from the Comptroller
- Work of the Charter Review Committee

8/6/2007

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## Disclosure Process

- Establishment of the Disclosure Practices Working Group (DPWG)
- Provide DPWG's Disclosure Controls & Procedures
- Cross-disciplinary internal working group
- City will take under advisement "shelf-like" disclosure system

8/6/2007

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## Next Steps

- Receive Audit Committee Comments
- Inform SEC of anticipated September response
- Present "final" letter to Council Sept. 4<sup>th</sup>
- Mail letter

8/6/2007

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OFFICE OF MAYOR JERRY SANDERS  
CITY OF SAN DIEGO

MEMORANDUM

Date: October 5, 2006

To: Honorable Members of the City Council

From: Mayor Jerry Sanders *[Signature]*

Subject: Kroll Remediation Status for October 16, 2006, Council Meeting

In my memorandum dated August 24, 2006, I reported my staff had identified 121 items for remediation from the Kroll Report. These items were grouped by remedial category and were described in detail along with anticipated due dates. On October 16, 2006, my staff will meet with you to discuss the following:

- Status of remedial items identified for completion in September 2006 (items 1-6, 46-47, 48.ii, 84-86)
- Status of the implementation of the organizational structure for financial operations (addresses items 7-14)
- Additional remedial items identified (items 4.1, 20.1, 52.1, 52.2, 57.1, 107.1, 118.1, 120.1)

The numbering convention for the additional remedial items follows the remedial categories identified in my August 24, 2006, memorandum. For example, "new" item 4.1 matches the remedial category of Oversight Monitor and is most closely associated with item 4 from my prior memorandum.

Attachment A – Financial Operations Organizational Charts

Cc: City Attorney  
BA  
Chief Operating Officer  
Chief Financial Officer  
SDCERS  
John Dyer

## I - Remedial Items due September 2006

### A. Completed Items

#### **Remedial Category – City Actuarial Services**

46. The City should periodically, but no less frequently than every three years, retain its own actuary to review the SDCERS actuarial valuation and the assumptions used, and to provide an independent assessment of the valuation and its implications for the City. (Pages 260, M-11 & M-12)
47. The City must retain its own actuary responsible for determining for the City the cost of each proposed new retirement benefit and to issue a report thereon to the City Council before an ordinance is adopted conferring the benefit. (Pages 260 & M-12)

**Status:** Complete. The City has retained an actuary, Joseph Esuchanko. The City's actuary is nearly complete with his first report. The delay in his completion is the result of additional work assigned by the City in order to assist with the calculation of the City's Net Pension Obligation for the 2003 CAFR. Revised due date for the report is November 2006.

#### **Remedial Category – Deferred Maintenance**

48. We recommend that the Mayor and the Budget Director establish a process to identify and prioritize deferred maintenance and unfunded procurement needs. The Budget Director should prepare and present a public report identifying cumulative deferred maintenance and unfunded procurement needs during the annual budget hearings. The City's approach to funding deferred maintenance and unfunded procurement should be changed to allow for increased funding in these areas. (Page M-21)

In responding to this item, the Mayor's August 24, 2006, memorandum identifies four specific components (i, ii, iii and iv). Only items i and ii are addressed below.

- i. (48.i) Development of a Facility Category Index to identify facilities and assets critical to the mission of the City and prioritize those assets for funding to address deferred maintenance requirements.

**Status:** Complete. The due date indicated in my August 24, 2006, memorandum for this item should have been September 2006 instead of September 2007. This date was transposed with item 48.ii.

- ii (48.ii) Development of an asset inventory to create current inventories of essential infrastructure assets (e.g., Chiller Plants, Boilers, Pumps, High Voltage Switch Gear).

**Status:** Not complete. The due date for this item was misstated as September 2006. The correct due date is September 2007.

## I - Remedial Items due September 2006

### B. In Process Items

#### **Remedial Category - Oversight Monitor**

1. Appoint a Monitor to oversee the implementation of and compliance with the Remediation Plan. (Pages 263 & M-14)
2. The Monitor should be selected by the Mayor in consultation with the City Council and subject to the approval of the SEC and should be an independent person of suitable standing, independence and experience for the assignment. (Pages 263 & M-14)
3. The Monitor should have complete and unfettered access to all City and SDCERS personnel and records. (Pages 263 & M-14)
4. The Monitor should make quarterly reports to the City and the SEC on the City's progress. (Pages 263 & M-14)
5. The Monitor should serve a term of no less than three years and should be provided adequate resources to carry the duties of his office. (Pages 263 & M-14)
6. The SEC should have the right, upon request, to expand the scope of the Monitor's duties following consultation with the City. (Pages 263 & M-14)

**Status:** In process. The appointment of an SEC approved Monitor is a recommendation that the Mayor supports. Further discussion with Council and the City Attorney's Office is needed to determine the term of retention and scope of duties. That discussion will occur prior to the November 13th, 2006, Council date, where a detailed presentation will be made.

#### **Remedial Category - Reconciliation of Accounts**

84. The City must develop an improved cash reconciliation process, which is more automated, documented, and complete. The revised process must support accuracy, timely completion, and improved ease of review. (Page M-16)
85. The City should develop and implement a timely and less cumbersome bank reconciliation process to clearly reconcile bank and the general ledger balances. The improved process should facilitate timely completion, ease of review, correction of errors, and enhance communication between the Comptroller's and Treasurer's staff. (Page M-16)

**Status:** In process. Cash for fiscal years 2003 and 2004 have been reconciled and reported to the City's external auditors. The establishment of a formal documented process will be complete by November 2006.

## I - Remedial Items due September 2006

86. City Departments should reconcile all accounts receivable and deferred revenue accounts to supporting information at period ends. Supervisors should review these reconciliations for completeness and accuracy. (Page M-23)

**Status:** In process. This is a significant task requiring reconciliations by each City department with material revenue. The process documentation for reconciling accounts receivable and deferred revenue to supporting information for each period needs to be updated. Subsequently, appropriate City employees require training on the process. Finally, the processes (by department) need to be tested to confirm operating effectiveness. Revised completion date is June 2007.



## II – Status of the Implementation of the Organizational Structure for Financial Operations

### Remedial Category – Organizational Structure

7. Centralize accountability for the accuracy and credibility of the City's financial reporting under the CFO. The areas of responsibility would include, a City Comptroller, a Director of Financial Reporting, the Financial Management Director, Director of Debt Management and City Treasurer. (Pages 245 & M-1)

**Status:** Completed. Prior to January 2006, the City's financial reporting structures were distributed throughout the organization. Some reported up to the City Manager through a Deputy and Assistant City Manager while the City Auditor & Comptroller, a separate department, reported to the Mayor and Council. This structure did not promote coordination, communications, accountability or transparency. One of the first changes I made upon taking office was to create the position of Chief Financial Officer (CFO) who is responsible for what I am calling the Department of Finance. The CFO is ultimately accountable for the accuracy and credibility of the City's financial reporting.

See organizational chart in Attachment A, 2006 Department of Finance. The City Comptroller (Auditor & Comptroller), Director of Financial Reporting (Financial Management), Director of Debt Management (Debt Management), and City Treasurer (Treasury) report directly to the CFO.

8. The Director of Planning, Budgeting and Financial Analysis (Financial Management Director) should report directly to the CFO and have principal responsibility for preparing an annual budget, a monthly budget with comparisons of budget to actual results year-to-date, analyses of variances and a quarterly report to the City Council and public setting forth budget versus actual results. (Pages 246 & M-2)

**Status:** Completed. The Financial Management Director reports directly to the CFO and has primary responsibility for preparing the annual budget. Quarterly reports have been provided to the City Council and public.

9. The City Treasurer should report to the CFO and have principal responsibility for all treasury functions for the City. (Pages 246 & M-2)
10. The CFO should have primary responsibility for, and have as direct reports, personnel with functional authority over accounting and financial analysis, treasury, planning and budgeting and financial reporting. This should include authority over those responsible for all information systems required by these functions. (Page M-1)
11. The Budget Director should report directly to the CFO and have principal responsibility for preparing an annual budget, a monthly budget with comparisons of budget to actual results year-to-date, analyses of variances, and a quarterly report to the City Council and public setting forth budgeted versus actual results. The Budget Director's Office should serve as a resource for financial analysis, planning assistance, and services to other City departments and agencies. (Page M-2)

## II – Status of the Implementation of the Organizational Structure for Financial Operations

12. The City Treasurer should report to the CFO and have principal responsibility for all treasury functions for the City. The Office of the Treasurer and the duties assigned to that Office shall be as otherwise described in the City Charter. (Page M-2)

**Status:** Completed. The City Treasurer and the Budget Director report directly to the CFO. The CFO has authority over accounting and financial analysis, treasury, fiscal planning, budgeting and financial reporting and the systems that support these responsibilities. See organizational charts in Attachment A.

13. Establish the position of City Comptroller responsible for accounting and financial reporting, including preparation of the CAFRs and reporting to the CFO. (Pages 245, 246 & M-2)

14. Establish the position of Director of Financial Reporting responsible for the preparation of the City's periodic financial statements. (Pages 246 & M-2)

**Status:** The establishment of a Comptroller position will require a City Charter change. Anticipated ballot date is June 2008. Currently, the duties outlined for the Director of Financial Reporting are the shared responsibility of the Auditor & Comptroller and the Financial Management Director. More distinct delineation of duties will be established once the Director of Financial Reporting position has been created.

### III – Additional Remedial Items Identified

Since the delivery of my August 24, 2006, memorandum on "Responses to the Remedial Recommendations Found in the Kroll Report," staff has combed through the Kroll Report an additional time and has identified a number of additional recommendations. Most of these closely tie to remedial recommendations already identified and often provide some additional clarity. These additional items are discussed below. As discussed in my cover memorandum to this document, any number listed below that is a whole number (i.e., 4, 20, 52, etc.) reflect remedial recommendations previously identified. The other numbers that follow (i.e., 4.1, 20.1, 52.1, 52.2, etc.) represent newly reported items.

#### **Remedial Category – Oversight Monitor**

- 4. Original Item. The Monitor should make quarterly reports to the City and the SEC on the City's progress. (Pages 263 & M-14)
- 4.1. Additional Item. City Monitor quarterly reports should be made public in an appropriate manner including on the City's website. (Page M-14)

**Response:** After the City appoints a Monitor and receives quarterly reports on the progress of implementation, these reports will be made public on the City's website.

#### **Remedial Category – Audit Committee, Formation and Duties**

- 20. Original Item. The Audit Committee should establish a written charter. (Pages 251 & M-6)
- 20.1. Additional item. The City's Audit Committee should approve the annual compensation of the Auditor General and the annual budget for the Auditor General's staff. (Page M-5)

**Response:** Requires City Charter Change. Due date is June 2008.

#### **Remedial Category – Disclosure**

- 52 Original Item. The City Council should have at least two weeks to review substantially completed drafts of a preliminary offering statement before it is asked to vote to approve the final document. (Pages 263 & M-14)
- 52.1. Additional Item. The City Council members should also establish a reasonable period of time for the review of a final offering statement document, with marked changes from earlier drafts. (Page M-14)
- 52.2 Additional Item. The City CAFR is an integral component of the financial information provided as part of any debt issuance; the City Council should review and approve its use following the same procedures as offering statements. (Page M-14)

### III – Additional Remedial Items Identified

**Response:** City Council should establish a reasonable period of time by December 31, 2006.

#### **Remedial Category – Financial Reporting**

57 Original Item. At year-end, a budget should be presented to the City Council containing a final budget-to-actual comparison, along with an explanation of variances by department. (Pages 262 & M-13)

57.1 Additional Item. Inter-departmental transfers to meet budget goals, or for any other purpose, should not be permitted unless approved in advance by the City Council. (Page M-13)

**Response:** It is staff's position that this has been implemented. First, the Appropriation Ordinance has been modified to remove the kind of flexibility to move funds around that were given the City Manager and Auditor and Comptroller in prior fiscal years. In addition, the City Council, through the Business Process Re-engineering (BPR) Ordinance still has the authority to review and take action on any and all movement of funds which result from BPRs prior to staff's processing any transfers. The City Council will be asked to approve the ultimate movement of funds via an amendment to the Appropriation Ordinance periodically throughout the fiscal year.

#### **Remedial Category – City Funding of SDCERS**

107 Original Item. The City and SDCERS should make a voluntary disclosure through a self-reporting process to the IRS of the amount of any improper diversion of funds used to pay retiree health care benefits and cooperate with the IRS to bring the City's retiree healthcare funding into full compliance. (Pages 259 & M-11)

107.1 Additional Item. Make early disclosure of such costs (retiree healthcare benefits) in its next issued financial statement. (Page M-11)

**Response:** While the City has not published the Net OPEB Obligation on its balance sheet, it has disclosed its actuarially developed liability in the transmittal letter of the fiscal year 2003 CAFR. It will do the same in all subsequent CAFRs and will begin reporting its Net OPEB Obligation in fiscal year 2008.

#### **Remedial Category – SDCERS Board Structure**

118 Original Item. Prior to any appointment, each potential appointee be required to complete a written application listing qualifications for the position and any factors that may impact on that decision, and that the applicants be required to affirm the accuracy of the application and a background check of the applicants should be done by the appropriate City department. (Pages 256 & M-9)

118.1 Additional Item. SDCERS board applications should be shared with the Business and Governance Committee of the SDCERS board. (Page M-9).

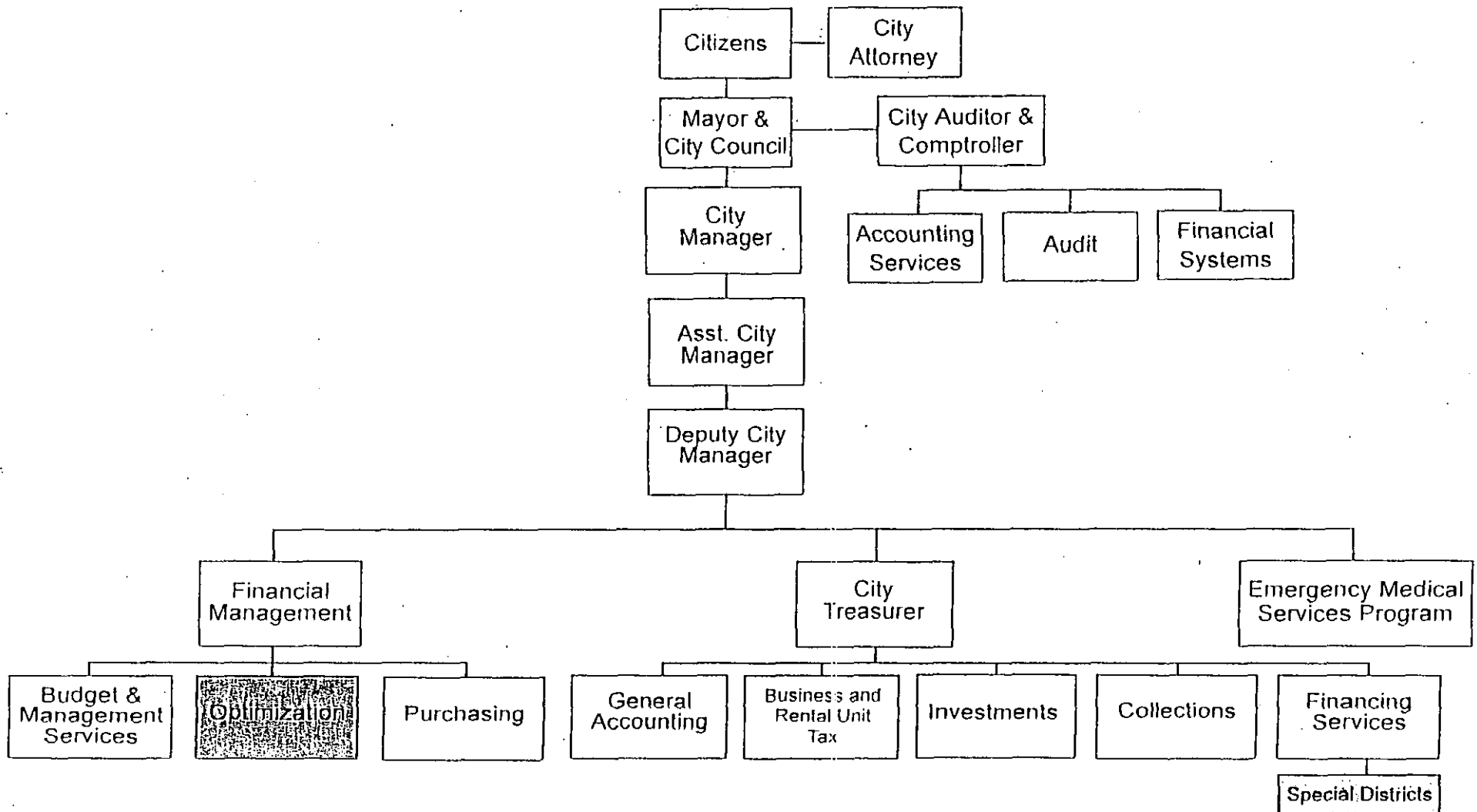
Response: City staff will work with SDCERS.

120 Original Item. SDCERS should adopt a formal charter for each committee which should be updated no less frequent than every three years. Pages 257 & M-9)

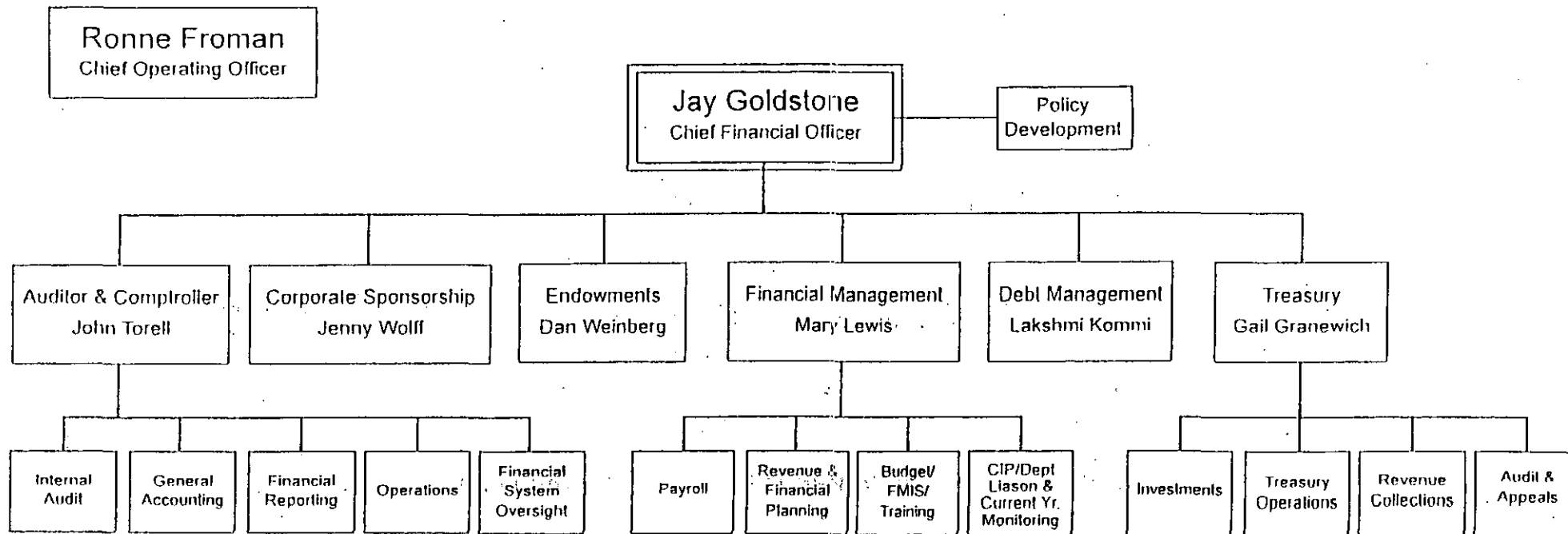
120.1 Additional Item. The annual SDCERS CAFR should include a report from each of its standing committees on significant activities during the year. (Page M-9)

Response: Staff will work with SDCERS staff.

# FINANCIAL MANAGEMENT 2005



## 2006 DEPARTMENT OF FINANCE

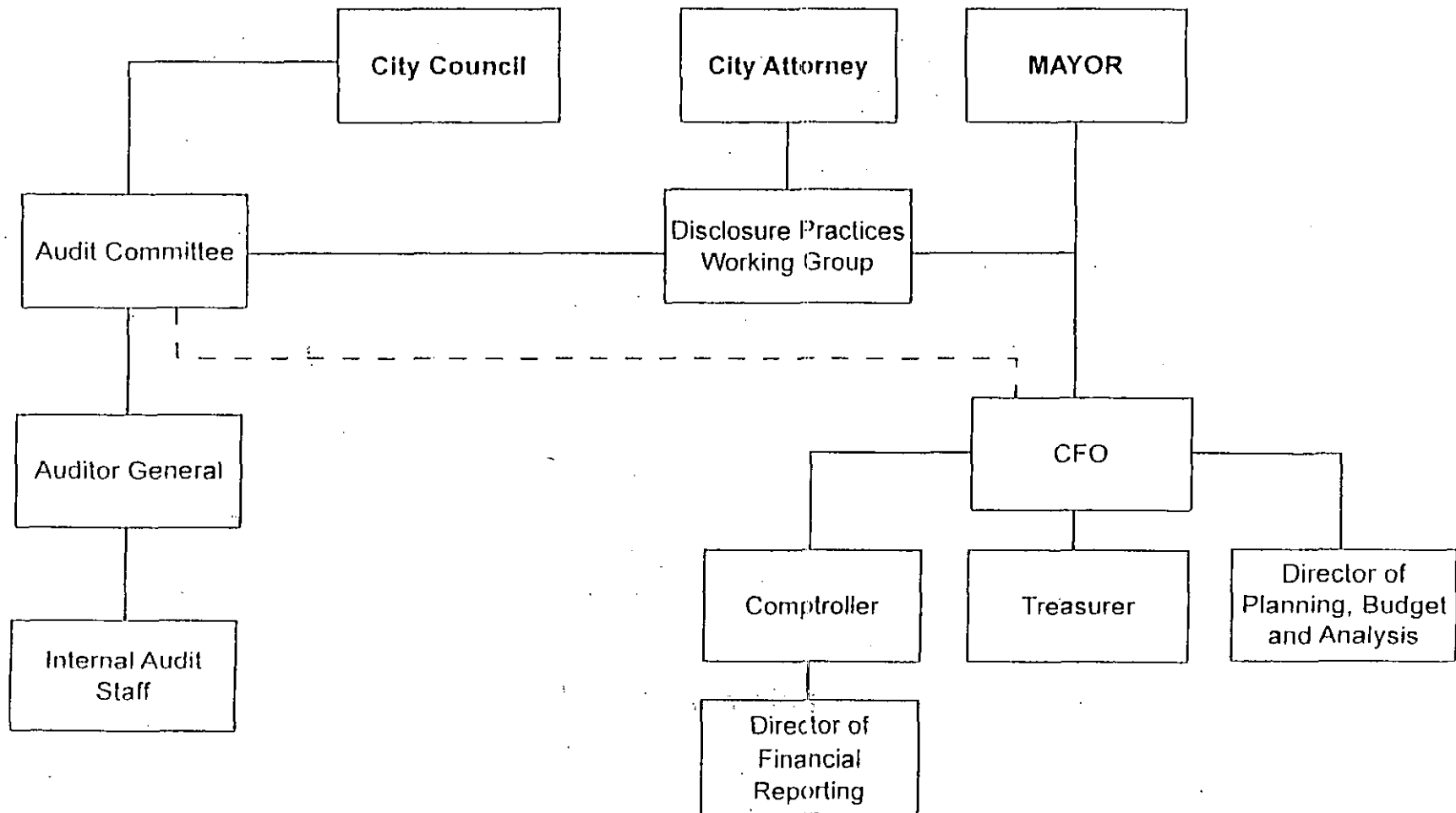


# APPENDIX N

## OF THE KROLL REPORT

### PROPOSED FINANCIAL REPORTING REORGANIZATION

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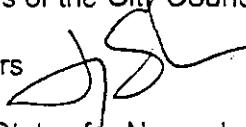
NOTE: Support to the Audit Committee would be provided by the CFO and Auditor General and their Staffs.





**OFFICE OF MAYOR JERRY SANDERS  
CITY OF SAN DIEGO**

**MEMORANDUM**

Date: October 30, 2006  
To: Honorable Members of the City Council  
From: Mayor Jerry Sanders   
Subject: Kroll Remediation Status for November 13, 2006, Council Meeting

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In my memorandum dated August 24, 2006, I reported my staff had identified 121 items for remediation from the Kroll Report. These items were grouped by remedial category and were described in detail along with anticipated due dates. In my memorandum dated October 5, 2006, I updated you on the status of items due in September 2006. On November 13, 2006, my staff will meet with you to discuss the following:

- Status of remedial items completed as of November 13, 2006.
- Status of remedial items in-process but not complete as of November 13, 2006

Attachment A – Mayor's memorandum dated October 5, 2006, Kroll Remediation Status for October 16, 2006, Council Meeting

Attachment B – City Employee Waste, Fraud, Abuse and Ethics Hotline Policy and Procedures Manual (Draft)

Attachment C – Anonymous Submission of Suspected Wrongdoing (Whistleblowers) – Issues for Government Audit Committees to Consider (source: AICPA)

Attachment D – Interest Allocation Remedial Documentation

Cc: City Attorney  
Chief Operating Officer  
Chief Financial Officer  
Independent Budget Analyst  
SDCERS  
John Dyer

## I. Remedial Items Completed

### A. Items Previously Reported Complete

Kroll Items 7-12, 46-47, 48(i), 57.1, 107.1 – see my memorandum dated October 5, 2006 (refer to Attachment A)

### B. Items Completed During this Reporting Period

#### Remedial Category – Audit Committee – Formation and Duties

24. The Audit Committee should have responsibility for the establishment and monitoring of effective policies and procedures for dealing with "whistleblower" complaints, including an internal hotline. (Pages 252 & M-6)

Status: Mayoral Office of Ethics and Integrity (OEI) task complete; awaiting meet and confer process results and formation of Audit Committee, see section II.B. The OEI has drafted a policy and procedures for the City's hotline process. Refer to Attachment B. In drafting the policy and procedures, the OEI used the American Institute of Certified Public Accountants (AICPA) tool kit for "Anonymous Submission of Suspected Wrongdoing (Whistleblowers) - Issues for Government Audit Committees to Consider." Refer to Attachment C.

The policy and procedures include protection for whistleblowers and meets the recommendations of Kroll Report item 24. The OEI is in the process of "meet and confer" with the City's unions regarding the policy and procedures manual. Once the Audit Committee is in place, the policy and procedures will be reviewed by the Committee and changed if necessary (after "meet and confer" with the unions).

#### Remedial Category – Budget Policies and Practices

45. The City should publish, along with the annual budget, the significant assumptions that can materially affect the budget, and a comparison of these assumptions against actual experience in recent years. (Pages 261 & M-12)

Status: Complete. The City's Fiscal Year (FY) 2007 budget is complete and will be distributed in November. Included in this document is a section that describes the assumptions used to develop the budget. As the City develops its first five-year financial plan, the projections for the current fiscal year will be frequently updated. This will provide a working tool for the City Council to compare budgeted assumptions to actual data.

The City of San Diego does not have actual data for FYs 2003-2005 to illustrate actual experience against the budget. In preparation of the FY 2008 budget and subsequent FY budgets, significant assumptions will be compared against actual experience for prior years.

## I. Remedial Items Completed

### Remedial Category – Financial Reporting

54. The City budget should be presented by month, by department. (Pages 261 & M-13)
55. At least quarterly, a report should be prepared reflecting budget-to-actual comparisons by department in aggregate, with an explanation of significant variances, to be disseminated to the public. (Pages 261 & M-13)
56. The City budget should present budget-to-actual comparisons by department, fiscal year-to-date, along with variances on a monthly basis. (Pages 261 & M-13)
57. At year-end, a budget should be presented to the City Council containing a final budget-to-actual comparison, along with an explanation of variances by department. (Pages 262 & M-13)

**Status:** Complete. The City budget by month, by department for the first two accounting periods was provided to the City Council and presented to the Budget and Finance Committee on October 18, 2006. This report also contains budget to actual comparisons and an explanation of significant variances. The report was made public on the City's website. A similar report will be published on a quarterly basis. Additionally, on September 13, 2006, The Fiscal Year 2006 Summary Report was presented to the City Council. This report contains a final budget-to-actual comparison, along with explanations of variances by department.

### Remedial Category – Interest Allocation

74. The City must develop an improved cash reconciliation process, which is more automated, documented, and complete. The revised process must support accuracy, timely completion, and improved ease of review. (Page M-16)

**Status:** Complete (internal control operating effectiveness to be tested by March 31, 2007). A formal documented process has been completed. Documentation includes an internal control matrix, process flow, process narrative and identification of significant control activities. Additionally, remediation documentation contains a background discussion, actions taken for remediation, design effectiveness assessment, operating effectiveness assessment and process improvement recommendations. Refer to Attachment D. The CFO briefed Macias Ginii & O'Connell on the remediation documentation and received positive feedback.

### Remedial Category – Reconciliation of Accounts

84. The City must develop an improved cash reconciliation process, which is more automated, documented, and complete. The revised process must support accuracy, timely completion, and improved ease of review. (Page M-16)

## I. Remedial Items Completed

85. The City should develop and implement a timely and less cumbersome bank reconciliation process to clearly reconcile bank and the general ledger balances. The improved process should facilitate timely completion, ease of review, correction of errors, and enhance communication between the Comptroller's and Treasurer's staff. (Page M-16)

Status: Complete (internal control operating effectiveness to be tested by March 31, 2007). A formal documented process has been completed. Documentation includes an internal control matrix, process flow, process narrative and identification of significant control activities.

Additionally, remediation documentation contains a background discussion, actions taken for remediation, design effectiveness assessment, operating effectiveness assessment and process improvement recommendations.

## II. Remedial Items In-Process

### A. Items In-Process Previously Reported

Kroll Items 1-6 and 86 – see my memorandum dated October 5, 2006 (refer to Attachment A).

There is no update to the status of Kroll item 86. Updated status for Kroll Items 1-6 is presented below.

#### **Remedial Category - Oversight Monitor**

1. Appoint a Monitor to oversee the implementation of and compliance with the Remediation Plan. (Pages 263 & M-14)
2. The Monitor should be selected by the Mayor in consultation with the City Council and subject to the approval of the SEC and should be an independent person of suitable standing, independence and experience for the assignment. (Pages 263 & M-14)
3. The Monitor should have complete and unfettered access to all City and SDCERS personnel and records. (Pages 263 & M-14)
4. The Monitor should make quarterly reports to the City and the SEC on the City's progress. (Pages 263 & M-14)
5. The Monitor should serve a term of no less than three years and should be provided adequate resources to carry the duties of his office. (Pages 263 & M-14)
6. The SEC should have the right, upon request, to expand the scope of the Monitor's duties following consultation with the City. (Pages 263 & M-14)

**Updated Status:** In process. Meetings are being scheduled with the Council and the City Attorney to discuss the Kroll recommended monitor. The Mayor will bring forward a monitor recommendation(s) as soon as possible but no later than January 31, 2007. The scope of duties, term of retention and qualifications will be consistent with the Kroll Report and any subsequent SEC order, if applicable. The Council will have the final approval over the term of retention, scope of duties and qualifications through approval of the contract entered into between the City and the monitor.

### B. Items In-Process During this Reporting Period

#### **Remedial Category – Audit Committee, Formation and Duties**

18. The City should establish a three member Audit Committee comprised of two members from the public and one City Council Member. The public members would be nominated by the Mayor and confirmed by the City Council. (Pages 251 & M-6)

## II. Remedial Items In-Process

19. The City's Financial Reporting Oversight Board should be eliminated as redundant to the Audit Committee. (Page M-6)
20. The Audit Committee should establish a written charter. (Pages 251 & M-6)
21. The Audit Committee should meet quarterly, or more often if necessary, with the City's independent auditors, the City's Auditor General and the CFO. (Page 252)
22. The Mayor, CFO, City Attorney, *Independent Budget Analyst (added)* and City Council should have the authority to make requests of the Audit Committee and Auditor General to perform internal audits of material matters they reasonably believe to be warranted. (Page 252)
23. With the assistance of the CFO and Auditor General, the City's independent auditors would be retained by, report to and take direction from the Audit Committee. (Page 252)
24. The Audit Committee should have responsibility for the establishment and monitoring of effective policies and procedures for dealing with "whistleblower" complaints, including an internal hotline. (Pages 252 & M-6)

### Status:

Long Term Plan – A City Charter change is required to fully meet all the Kroll Report Audit Committee recommendations identified above. The Mayor requests the City Council direct the City Attorney to prepare a proposed Charter change that will meet the Kroll Report recommendations. The proposed Charter change should be included in the June 2008 general election.

Short Term Plan – Until the above Charter change can be effectuated, the Mayor requests the City Council direct the City Attorney to amend the Municipal Code<sup>1</sup>, using the Kroll Report language as modified below, to convert the Financial Reporting Oversight Board into the Advisory Audit Committee which will serve as an advisory board to the Mayor and City Council.

Sec 1472  
behind A# 0

18. The City should establish a three member Audit Committee comprised of two members from the public and one City Council Member. The public members would be nominated by the Mayor and confirmed by the City Council. (Pages 251 & M-6) No change.
19. The City's Financial Reporting Oversight Board should be eliminated as redundant to the Audit Committee. (Page M-6) No change.
20. The Audit Committee should establish a written charter consistent with its role as an advisor to the Mayor and City Council. (Pages 251 & M-6)

<sup>1</sup> San Diego Municipal Code, Chapter 2: Government, Article 6: Board and Commissions, Division 17: Financial Reporting Oversight Board

## II. Remedial Items In-Process

21. The Audit Committee, in conjunction with the Mayor and City Attorney, should meet quarterly, or more often if necessary, with the City's independent auditors, the City's Auditor General and the CFO. (Page 252)
22. The Mayor, CFO, City Attorney, *Independent Budget Analyst (added)* and City Council should have the authority to make requests of the Audit Committee and Auditor General to perform internal audits of material matters they reasonably believe to be warranted. (Page 252) No change.
23. With the assistance of the CFO and Auditor General, the City's independent auditors would be retained by, report to and take direction from the Mayor and City Council. The Audit Committee will provide input on an advisory basis. (Page 252)
24. The Audit Committee, in an advisory capacity to the Mayor and City Council, should have responsibility for the establishment and monitoring of effective policies and procedures for dealing with "whistleblower" complaints, including an internal hotline. (Pages 252 & M-6)

### Remedial Category – Ethics

42. To discourage any improper influence of the professionals who serve as "gatekeepers" to the public financial reporting process of the City, the Municipal Code should be amended to add criminal penalties for such conduct. It should be unlawful for any elected official, or employee of the City, or anyone acting under their direction, to take any action to corruptly influence, coerce, manipulate or mislead any independent certified public accountant engaged in the performance of an audit of the financial statements of the City or its component units, or outside legal counsel performing services for the City in connection with an offering statement of the City, or any actuary performing an actuarial valuation in connection with the preparation of the City's or SDCERS's CAFRs, or employees of a bond rating agency performing a credit rating of the City's bonds. (Page M-6)

Status: Waiting promised Ordinance from City Attorney's office.

### Remedial Category – Budget Policies and Practices

43. In order to maintain current service levels and address issues such as deferred maintenance, the City must reduce expenditures by improving efficiency, increasing the current revenue base, and seeking alternative revenue sources. (Page M-14)

Status: As the City develops its first five-year financial plan, it will address current service levels and other budgetary demands.

## II. Remedial Items In-Process

44. Ongoing expenditures should be supported by ongoing revenues; capital projects should identify all future cost considerations and financial impacts, including direct and indirect costs for each Enterprise Fund; activities supported by user fees should be fully cost recoverable; discretionary General Fund revenues should not be earmarked; increase the General Fund reserve to the range of 7-10%; budget development should be guided by a long term or strategic plan proposed by the Mayor and adopted by the City Council; and after adoption, annual budgets should be amended only for urgent needs. Specific funding sources should be identified to pay for these needs. (Pages M-14 & M-15)

**Status:** A General Fund reserve policy will be presented to the Budget and Finance Committee at its November 29th Committee meeting and to the full Council for action at a subsequent meeting in December. The policy will identify a reserve account, separate from the "deep" reserves, which will serve as a contingency for unanticipated expenses approved by City Council during a given fiscal year.

### Remedial Category – Retirement Benefits

87. The City Council and employees should develop realistic retirement plan parameters for future City hires. This includes positioning the City to attract and retain the talent needed to meet the citizens' expectations for services, not be viewed as providing excessive benefit levels, and creating a plan the City can afford. (Page M-25)

**Status:** A benchmark study of health and retirement benefits for all employees is in process. Additionally, benchmark studies of police and fire compensation are in process.





OFFICE OF MAYOR JERRY SANDERS  
CITY OF SAN DIEGO

MEMORANDUM

Date: October 5, 2006

To: Honorable Members of the City Council

From: Mayor Jerry Sanders *[Signature]*

Subject: Kroll Remediation Status for October 16, 2006, Council Meeting

In my memorandum dated August 24, 2006, I reported my staff had identified 121 items for remediation from the Kroll Report. These items were grouped by remedial category and were described in detail along with anticipated due dates. On October 16, 2006, my staff will meet with you to discuss the following:

- Status of remedial items identified for completion in September 2006 (items 1-6, 46-47, 48.ii, 84-86)
- Status of the implementation of the organizational structure for financial operations (addresses items 7-14)
- Additional remedial items identified (items 4.1, 20.1, 52.1, 52.2; 57.1, 107.1, 118.1, 120.1)

The numbering convention for the additional remedial items follows the remedial categories identified in my August 24, 2006, memorandum. For example, "new" item 4.1 matches the remedial category of Oversight Monitor and is most closely associated with item 4 from my prior memorandum.

Attachment A – Financial Operations Organizational Charts

Cc: City Attorney  
BA  
Chief Operating Officer  
Chief Financial Officer  
SDCERS  
John Dyer

## I - Remedial Items due September 2006

### A. Completed Items

#### **Remedial Category – City Actuarial Services**

46. The City should periodically, but no less frequently than every three years, retain its own actuary to review the SDCERS actuarial valuation and the assumptions used, and to provide an independent assessment of the valuation and its implications for the City. (Pages 260, M-11 & M-12)
47. The City must retain its own actuary responsible for determining for the City the cost of each proposed new retirement benefit and to issue a report thereon to the City Council before an ordinance is adopted conferring the benefit. (Pages 260 & M-12)

**Status:** Complete. The City has retained an actuary, Joseph Esuchanko. The City's actuary is nearly complete with his first report. The delay in his completion is the result of additional work assigned by the City in order to assist with the calculation of the City's Net Pension Obligation for the 2003 CAFR. Revised due date for the report is November 2006.

#### **Remedial Category – Deferred Maintenance**

48. We recommend that the Mayor and the Budget Director establish a process to identify and prioritize deferred maintenance and unfunded procurement needs. The Budget Director should prepare and present a public report identifying cumulative deferred maintenance and unfunded procurement needs during the annual budget hearings. The City's approach to funding deferred maintenance and unfunded procurement should be changed to allow for increased funding in these areas. (Page M-21)

In responding to this item, the Mayor's August 24, 2006, memorandum identifies four specific components (i, ii, iii and iv). Only items i and ii are addressed below.

- i. (48.i) Development of a Facility Category Index to identify facilities and assets critical to the mission of the City and prioritize those assets for funding to address deferred maintenance requirements.

**Status:** Complete. The due date indicated in my August 24, 2006, memorandum for this item should have been September 2006 instead of September 2007. This date was transposed with item 48.ii.

- ii (48.ii) Development of an asset inventory to create current inventories of essential infrastructure assets (e.g., Chiller Plants, Boilers, Pumps, High Voltage Switch Gear).

**Status:** Not complete. The due date for this item was misstated as September 2006. The correct due date is September 2007.

B. In Process Items

**Remedial Category - Oversight Monitor**

1. Appoint a Monitor to oversee the implementation of and compliance with the Remediation Plan. (Pages 263 & M-14)
2. The Monitor should be selected by the Mayor in consultation with the City Council and subject to the approval of the SEC and should be an independent person of suitable standing, independence and experience for the assignment. (Pages 263 & M-14)
3. The Monitor should have complete and unfettered access to all City and SDCERS personnel and records. (Pages 263 & M-14)
4. The Monitor should make quarterly reports to the City and the SEC on the City's progress. (Pages 263 & M-14)
5. The Monitor should serve a term of no less than three years and should be provided adequate resources to carry the duties of his office. (Pages 263 & M-14)
6. The SEC should have the right, upon request, to expand the scope of the Monitor's duties following consultation with the City. (Pages 263 & M-14)

**Status:** in process. The appointment of an SEC approved Monitor is a recommendation that the Mayor supports. Further discussion with Council and the City Attorney's Office is needed to determine the term of retention and scope of duties. That discussion will occur prior to the November 13th, 2006, Council date, where a detailed presentation will be made.

**Remedial Category - Reconciliation of Accounts**

84. The City must develop an improved cash reconciliation process, which is more automated, documented, and complete. The revised process must support accuracy, timely completion, and improved ease of review. (Page M-16)
85. The City should develop and implement a timely and less cumbersome bank reconciliation process to clearly reconcile bank and the general ledger balances. The improved process should facilitate timely completion, ease of review, correction of errors, and enhance communication between the Comptroller's and Treasurer's staff. (Page M-16)

**Status:** In process. Cash for fiscal years 2003 and 2004 have been reconciled and reported to the City's external auditors. The establishment of a formal documented process will be complete by November 2006.

I-- Remedial Items due September 2006

86. City Departments should reconcile all accounts receivable and deferred revenue accounts to supporting information at period ends. Supervisors should review these reconciliations for completeness and accuracy. (Page M-23)

Status: In process. This is a significant task requiring reconciliations by each City department with material revenue. The process documentation for reconciling accounts receivable and deferred revenue to supporting information for each period needs to be updated. Subsequently, appropriate City employees require training on the process. Finally, the processes (by department) need to be tested to confirm operating effectiveness. Revised completion date is June 2007.

## .. Status of the Implementation of the Organizational Structure for Financial Operations

### Remedial Category – Organizational Structure

7. Centralize accountability for the accuracy and credibility of the City's financial reporting under the CFO. The areas of responsibility would include, a City Comptroller, a Director of Financial Reporting, the Financial Management Director, Director of Debt Management and City Treasurer. (Pages 245 & M-1)

**Status:** Completed. Prior to January 2006, the City's financial reporting structures were distributed throughout the organization. Some reported up to the City Manager through a Deputy and Assistant City Manager while the City Auditor & Comptroller, a separate department, reported to the Mayor and Council. This structure did not promote coordination, communications, accountability or transparency. One of the first changes I made upon taking office was to create the position of Chief Financial Officer (CFO) who is responsible for what I am calling the Department of Finance. The CFO is ultimately accountable for the accuracy and credibility of the City's financial reporting.

See organizational chart in Attachment A, 2006 Department of Finance. The City Comptroller (Auditor & Comptroller), Director of Financial Reporting (Financial Management), Director of Debt Management (Debt Management), and City Treasurer (Treasury) report directly to the CFO.

8. The Director of Planning, Budgeting and Financial Analysis (Financial Management Director) should report directly to the CFO and have principal responsibility for preparing an annual budget, a monthly budget with comparisons of budget to actual results year-to-date, analyses of variances and a quarterly report to the City Council and public setting forth budget versus actual results. (Pages 246 & M-2)

**Status:** Completed. The Financial Management Director reports directly to the CFO and has primary responsibility for preparing the annual budget. Quarterly reports have been provided to the City Council and public.

9. The City Treasurer should report to the CFO and have principal responsibility for all treasury functions for the City. (Pages 246 & M-2)
10. The CFO should have primary responsibility for, and have as direct reports, personnel with functional authority over accounting and financial analysis, treasury, planning and budgeting and financial reporting. This should include authority over those responsible for all information systems required by these functions. (Page M-1)
11. The Budget Director should report directly to the CFO and have principal responsibility for preparing an annual budget, a monthly budget with comparisons of budget to actual results year-to-date, analyses of variances, and a quarterly report to the City Council and public setting forth budgeted versus actual results. The Budget Director's Office should serve as a resource for financial analysis, planning assistance, and services to other City departments and agencies. (Page M-2)

## II -- Status of the Implementation of the Organizational Structure for Financial Operations

12. The City Treasurer should report to the CFO and have principal responsibility for all treasury functions for the City. The Office of the Treasurer and the duties assigned to that Office shall be as otherwise described in the City Charter. (Page M-2)

**Status:** Completed. The City Treasurer and the Budget Director report directly to the CFO. The CFO has authority over accounting and financial analysis, treasury, fiscal planning, budgeting and financial reporting and the systems that support these responsibilities. See organizational charts in Attachment A.

13. Establish the position of City Comptroller responsible for accounting and financial reporting, including preparation of the CAFRs and reporting to the CFO. (Pages 245, 246 & M-2)

14. Establish the position of Director of Financial Reporting responsible for the preparation of the City's periodic financial statements. (Pages 246 & M-2)

**Status:** The establishment of a Comptroller position will require a City Charter change. Anticipated ballot date is June 2008. Currently, the duties outlined for the Director of Financial Reporting are the shared responsibility of the Auditor & Comptroller and the Financial Management Director. More distinct delineation of duties will be established once the Director of Financial Reporting position has been created.

### III – Additional Remedial Items Identified

Since the delivery of my August 24, 2006, memorandum on "Responses to the Remedial Recommendations Found in the Kroll Report," staff has combed through the Kroll Report an additional time and has identified a number of additional recommendations. Most of these closely tie to remedial recommendations already identified and often provide some additional clarity. These additional items are discussed below. As discussed in my cover memorandum to this document, any number listed below that is a whole number (i.e., 4, 20, 52, etc.) reflect remedial recommendations previously identified. The other numbers that follow (i.e., 4.1, 20.1, 52.1, 52.2, etc.) represent newly reported items.

#### **Remedial Category – Oversight Monitor**

4. Original Item. The Monitor should make quarterly reports to the City and the SEC on the City's progress. (Pages 263 & M-14)

- 4.1. Additional Item. City Monitor quarterly reports should be made public in an appropriate manner including on the City's website. (Page M-14)

Response: After the City appoints a Monitor and receives quarterly reports on the progress of implementation, these reports will be made public on the City's website.

#### **Remedial Category – Audit Committee, Formation and Duties**

20. Original Item. The Audit Committee should establish a written charter. (Pages 251 & M-6)

- 20.1. Additional item. The City's Audit Committee should approve the annual compensation of the Auditor General and the annual budget for the Auditor General's staff. (Page M-5)

Response: Requires City Charter Change. Due date is June 2008.

#### **Remedial Category – Disclosure**

- 52 Original Item. The City Council should have at least two weeks to review substantially completed drafts of a preliminary offering statement before it is asked to vote to approve the final document. (Pages 263 & M-14)

- 52.1. Additional Item. The City Council members should also establish a reasonable period of time for the review of a final offering statement document, with marked changes from earlier drafts. (Page M-14)

- 52.2 Additional Item. The City CAFR is an integral component of the financial information provided as part of any debt issuance; the City Council should review and approve its use following the same procedures as offering statements. (Page M-14)

### III -- Additional Remedial Items Identified

Response: City Council should establish a reasonable period of time by December 31, 2006.

#### **Remedial Category -- Financial Reporting**

57 Original Item. At year-end, a budget should be presented to the City Council containing a final budget-to-actual comparison, along with an explanation of variances by department. (Pages 262 & M-13)

57.1. Additional Item. Inter-departmental transfers to meet budget goals, or for any other purpose, should not be permitted unless approved in advance by the City Council. (Page M-13)

Response: It is staff's position that this has been implemented. First, the Appropriation Ordinance has been modified to remove the kind of flexibility to move funds around that were given the City Manager and Auditor and Comptroller in prior fiscal years. In addition, the City Council, through the Business Process Re-engineering (BPR) Ordinance still has the authority to review and take action on any and all movement of funds which result from BPRs prior to staff's processing any transfers. The City Council will be asked to approve the ultimate movement of funds via an amendment to the Appropriation Ordinance periodically throughout the fiscal year.

#### **Remedial Category -- City Funding of SDCERS**

107 Original Item. The City and SDCERS should make a voluntary disclosure through a self-reporting process to the IRS of the amount of any improper diversion of funds used to pay retiree health care benefits and cooperate with the IRS to bring the City's retiree healthcare funding into full compliance. (Pages 259 & M-11)

107.1 Additional Item. Make early disclosure of such costs (retiree healthcare benefits) in its next issued financial statement. (Page M-11)

Response: While the City has not published the Net OPEB Obligation on its balance sheet, it has disclosed its actuarially developed liability in the transmittal letter of the fiscal year 2003 CAFR. It will do the same in all subsequent CAFRs and will begin reporting its Net OPEB Obligation in fiscal year 2008.

#### **Remedial Category -- SDCERS Board Structure**

118 Original Item. Prior to any appointment, each potential appointee be required to complete a written application listing qualifications for the position and any factors that may impact on that decision, and that the applicants be required to affirm the accuracy of the application and a background check of the applicants should be done by the appropriate City department. (Pages 256 & M-9)



118.1 Additional Item. SDCERS board applications should be shared with the Business and Governance Committee of the SDCERS board. (Page M-9)

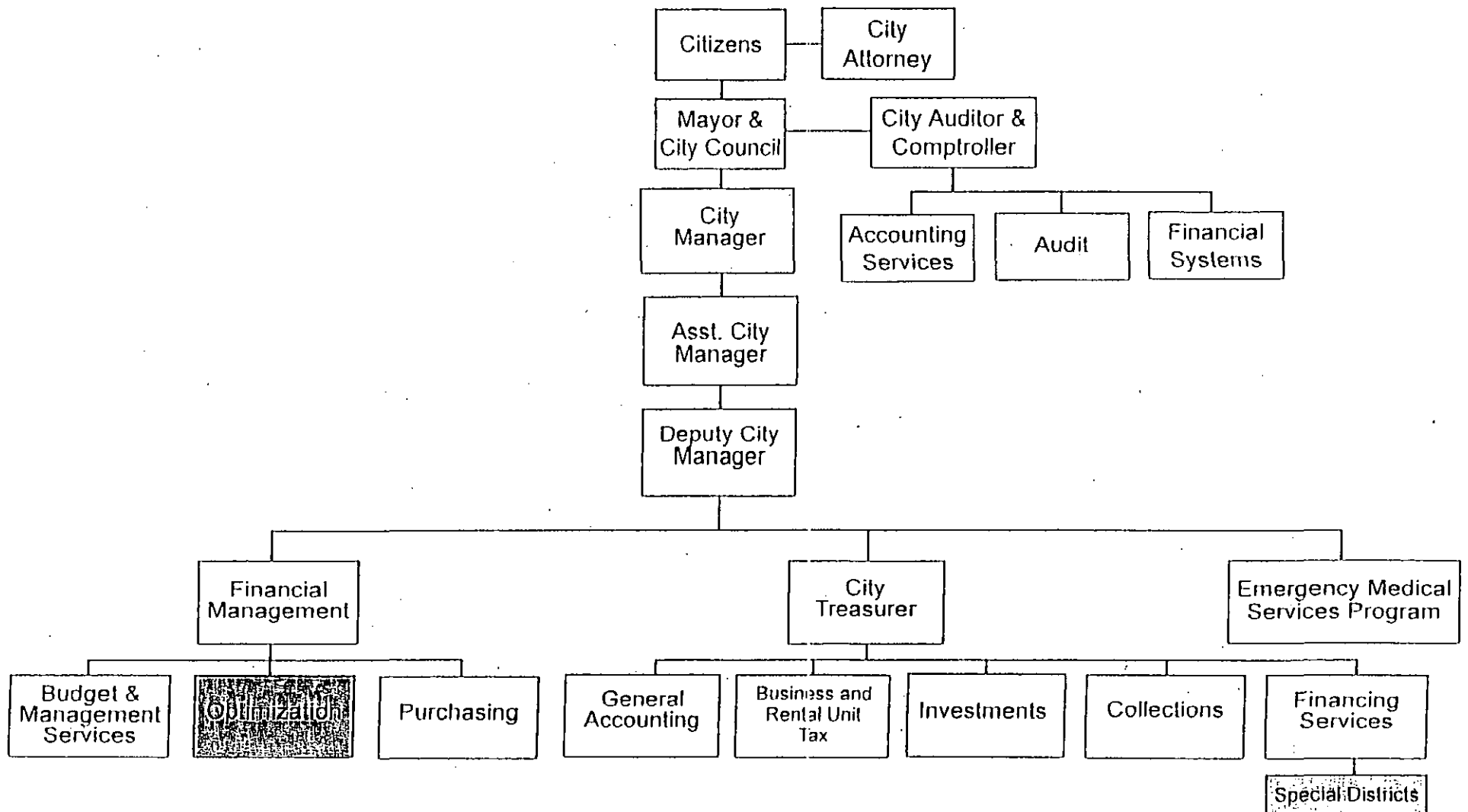
Response: City staff will work with SDCERS.

120 Original Item. SDCERS should adopt a formal charter for each committee which should be updated no less frequent than every three years. Pages 257 & M-9)

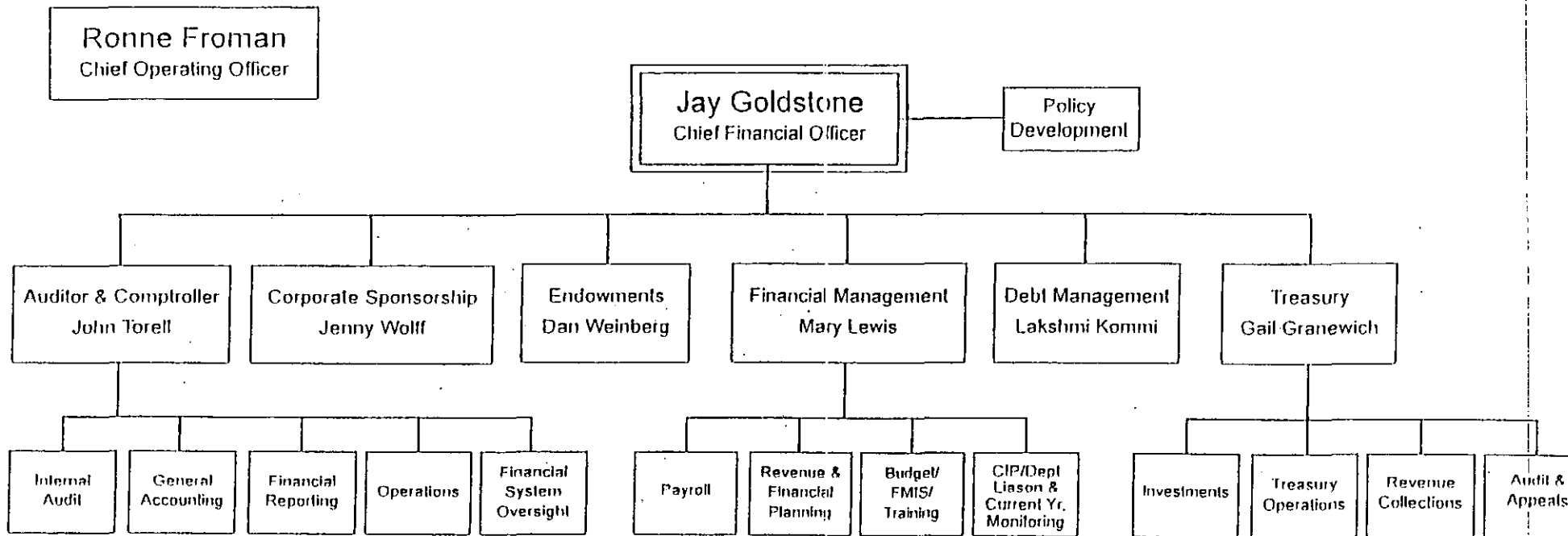
120.1 Additional Item. The annual SDCERS CAFR should include a report from each of its standing committees on significant activities during the year. (Page M-9)

Response: Staff will work with SDCERS staff.

# FINANCIAL MANAGEMENT 2005



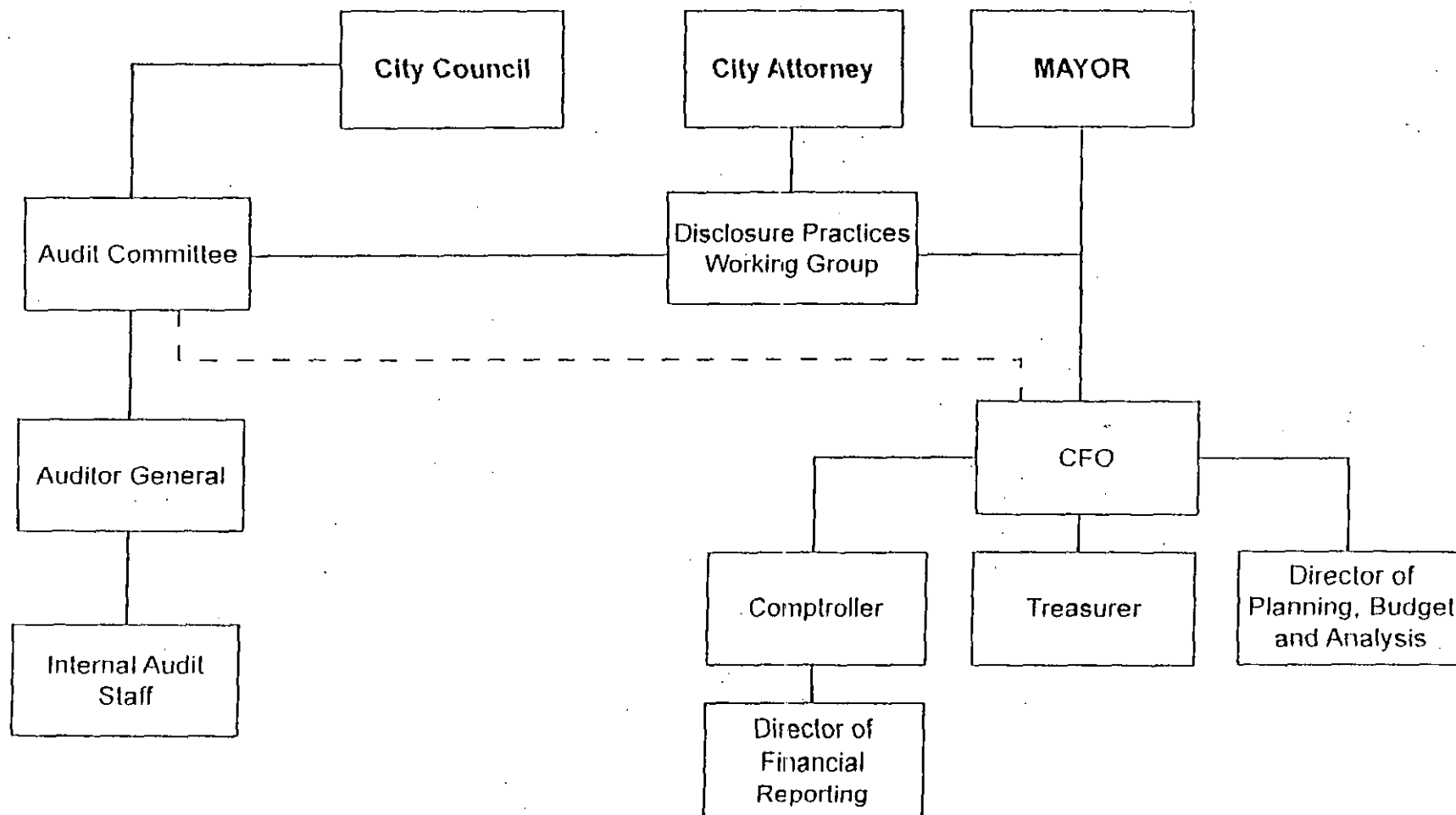
## 2006 DEPARTMENT OF FINANCE



# APPENDIX N

## OF THE KROLL REPORT

### PROPOSED FINANCIAL REPORTING REORGANIZATION



NOTE: Support to the Audit Committee would be provided by the CFO and Auditor General and their Staffs.

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City of San Diego  
***Office of Ethics and Integrity***

**Doing What's Right**

1-866-309-3500  
24 Hours A Day  
7 Days A Week  
365 Days A Year

City Employee  
Waste, Fraud, Abuse and Ethics Hotline  
Policy and Procedures Manual

Issued TBD

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OFFICE OF ETHICS AND INTEGRITY <i>Policies and Procedures Manual</i>	Page 2 of 27
City Employee Hotline and Complaint Program	Effective Date TBD

## Prelude

The purpose of the manual is to assist Department Directors or their designee, Agencies, and anyone involved in the Employee Hotline or citizen complaint investigations to ensure they understand their responsibilities. It is also intended to provide consistency among all parties involved in the management and conduct of Employee Hotline or citizen complaint investigations.

Office of Ethics and Integrity  
(619) 236 - 7072  
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<b>OFFICE OF ETHICS AND INTEGRITY</b> <i>Policies and Procedures Manual</i>	Page 3 of 27
City Employee Hotline and Complaint Program	Effective Date TBD

## I. Overview of the Employee Hotline and Complaint Program

### A. Introduction

<b>History</b>	In an investigative report authored by Vinson & Elkins L.L.P. (V&E Report) dated September 16, 2004, and adopted by San Diego City Council as San Diego Municipal Code §26.1703(c) in October 2004, recommendations were made to "establish procedures to receive and respond to any complaints or concerns regarding accounting, internal controls or auditing matters, including procedures for the confidential and anonymous submission by employees of any such complaints or concerns."
<b>Implementation of the Employee Hotline</b>	The Auditor and Comptroller's Office implemented the Employee Hotline (866-809-3500) on December 2, 2005, in response to San Diego Municipal Code §26.1703(c).
<b>OEI Role</b>	Upon the transition to the Strong Mayor form of Government on January 1, 2006, the Mayor's Office of Ethics and Integrity (OEI) was created and now, through a third-party provider, administers the Employee Hotline. As well, OEI directly accepts employee and citizen complaints.
<b>Objective</b>	The primary objective of the Employee Hotline/Complaint program is to provide a means for City of San Diego employees and citizens to confidentially report 1) any activity or conduct in which he/she suspects instances of fraud, waste, or abuse, 2) behavior not conducive to the City's ethical policies, rules and regulations, and 3) violations of certain federal or state laws and regulations (e.g., laws prohibiting discrimination or whistleblower laws).
<b>Structure</b>	With respect to the Employee Hotline, an independent third-party provider receives calls from City employees, providing complete confidentiality. The caller can choose to remain anonymous. The third-party provider



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issues reports for each call and submits the reports to OEI for review and referral.

Employees and citizens may also contact OEI directly via email ([oei@sandiego.gov](mailto:oei@sandiego.gov)) or by phone (619-236-7182). These communications are also treated confidentially.

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## B. Terms & Definitions

<b>Fraud</b>	A dishonest and deliberate course of action that results in the obtaining of money, property or an advantage to which the City employee or official committing the action would not normally be entitled. Intentional misleading or deceitful conduct that deprives the City of its resources or rights.
<b>Examples of Activities Involving Fraud (not an all-inclusive list)</b>	<ul style="list-style-type: none"> <li>• Falsifying financial records to misrepresent financial data or conceal the theft of money or City property.</li> <li>• Theft or misuse of City of San Diego money, equipment, supplies and/or other materials.</li> <li>• Intentionally misrepresenting the cost of goods and services provided.</li> <li>• Soliciting or accepting a bribe or kickback.</li> <li>• Falsifying payroll information.</li> </ul>
<b>Waste</b>	The intentional or unintentional, thoughtless or careless expenditure, consumption, mismanagement, use, or squandering of City resources. Waste also includes incurring unnecessary costs because of inefficient or ineffective practices, systems, or controls.
<b>Examples of Activities Involving Waste (not an all-inclusive list)</b>	<ul style="list-style-type: none"> <li>• Unnecessary spending of City funds to purchase supplies or equipment.</li> <li>• Failure to reuse or recycle major resources or reduce waste generation.</li> </ul>
<b>Abuse</b>	Intentional destruction, diversion, manipulation, misapplication, maltreatment, or misuse of City resources. Extravagant or excessive use as to abuse one's position or authority. Abuse can occur in financial or non-financial settings.
<b>Examples of Activities</b>	<ul style="list-style-type: none"> <li>• Failure to report damage to City equipment or property.</li> </ul>

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**Involving Abuse  
(not an all-  
inclusive list)**

- Receiving favor for awarding contracts to certain vendors.
- Using one's position in one City department to gain an advantage over another City resident or vendor when conducting personal business in another City department.

**Ethics Intake and  
Review  
Committee**

The Ethics Intake and Review Committee is composed of (1) the Deputy Chief Ethics and Integrity, (2) the Personnel Director, (3) the Auditor General or designee, and (4) the Ethics Audit and Compliance Specialist. This committee meets regularly to review complaints which have been made to OEI either through the Employee Hotline or by any other means.

**Governmental  
Ethics Laws**

Consist of the following: San Diego Municipal Code at Chapter 2, Article 7, Division 29 (Elections Campaign Control Ordinance); Chapter 2, Article 7, Division 35 (Ethics Ordinance); and Chapter 2, Article 7, Division 40 (Municipal Lobbying Ordinance).

The Ethics Commission enforces violations of the Election Campaign Control Ordinance, the Ethics Ordinance, and the Municipal Lobbying Ordinance.

**City Ethical  
Policies, Rules &  
Regulations**

City Charter sections, Administrative Regulations, Personnel Regulations, Council Policies, and City EEO Policy regarding subjects including:

- Avoidance of the Appearance of Impropriety
- Confidentiality
- Conflict of Interest
- Electronic mail and Internet Usage
- Employment of Relatives
- Future Employment
- Gifts/Favors
- Improper Use of Position
- Incompatible Employment
- Nondiscrimination
- Objective Contracting Process

<sup>1</sup> The Auditor General position is subject to Council and Voter Approval. In the interim, we will use the existing process that is analogous to the City.

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- Obligations to Citizens
- Participation in Political Activities
- Reporting Improper Conduct/Whistleblower Protection
- Sexual Harassment
- Use of City Resources for Private Gain

<b>Employee</b>	Any person who is employed by the City of San Diego.
<b>Complainant</b>	A party (employee or citizen) that lodges a complaint or concern, written or otherwise, with the Office of Ethics and Integrity.
<b>Complaint</b>	An expression of dissatisfaction or a cause or reason for complaining; a grievance filed by either an employee or citizen. Throughout the remainder of this manual "Complaint" will include Incident Reports resulting from an employee and/or citizen filing.
<b>Third-Party Provider</b>	An independent company (The Network, Inc.), which provides offsite, hotline coverage 24/7/365, with live interviewers who ask probative questions to gather necessary information to obtain actionable information. This information is then transcribed into a report.
<b>Incident Report</b>	The case management system converts the information received through the interview process into an organized report called an Incident Report. These reports are disseminated to OEI's designated recipients (See Section IV – Dissemination and Escalation Teams for further details).
<b>Summary Complaint Report</b>	A summary of all incident reports by type (e.g., policy issues, employee relations, customer relations) within a specified period of time. This report is available on the OEI website.
<b>Closed Hotline Calls Report</b>	A summary of all closed non-personnel incident reports within a specified time period. The Summary Complaint Report includes the date and time reports were received, incident types, and brief descriptions of the incidents. This report is available on the OEI website.

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**Case  
Management  
System**

The Network's online tool to facilitate a thorough interview that adapts to the issues identified in each call, and to the monitoring of investigations. It allows OEI to document all activities in a single, centralized system.

**Response**

A reply or an answer from the designated division or department head that addresses the following:

- A description of an *immediate* plan to address the issue/concern,
- Description of a plan to *prevent* the issue/concern from happening again, if warranted and
- Description of the resolution of the issue/concern.

**Audit Committee<sup>ii</sup>**

The Audit Committee is comprised of three-members, two are appointed by the Mayor from the public and confirmed by the City Council and one is a member of Council. The two public members should have expertise in accounting, auditing and financial reporting.

The purpose of the Audit Committee is:

- To ensure objective oversight of the City's financial reporting process;
- To monitor the performance of the City's internal audit function and Auditor General; and
- To retain the independent auditor, who will report to and take direction from, the audit committee.

<sup>ii</sup> The Audit Committee is subject to Council Approval. In the interim, we will use the existing process that is analogous to the City.

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#### **Auditor General<sup>1</sup>**

The Auditor General is nominated by the Mayor and confirmed by a majority of the City Council. The Auditor General is responsible for internal audits of the City's:

1. internal controls;
2. financial accounting, reporting and disclosure;
3. operations; and
4. incidents of fraud, waste and abuse.

#### **Citizens' Review Board of Police Practices**

The Citizens' Review Board of Police Practices:

- reviews and evaluates serious complaints brought by the public against officers of the Police Department of the City of San Diego;
- reviews all officer involved shootings and in-custody deaths; and
- reviews and evaluates the administration of discipline arising from sustained complaints.

<sup>1</sup> The Auditor General position is subject to Council and Voter Approval. In the interim, we will use the existing process that is analogous to the City.

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## II. Processing of Employee Hotline Complaints

1. A third-party provider shall receive and record all hotline calls through a designated toll-free number published to City employees. Information from such calls is recorded on an "Incident Report."
2. Upon completion of a complainant's call, the independent third-party provider sends an Incident Report via e-mail to the City's designated dissemination team, comprised of (1) the Deputy Chief Ethics and Integrity, (2) the Ethics Audit and Compliance Specialist, and (3) the Auditor General.<sup>1</sup> OEI Ethics Audit and Compliance Specialist shall be responsible for logging those complaints that come directly to the OEI's third-party's Case Management System. A copy of the incident reports will be forwarded to the Ethics Commission.
  - o The Ethics Commission Director reviews each report to determine if there exist factual allegations suggesting a violation of any governmental ethics laws. Nothing contained in these policies and procedures shall preclude the Ethics Commission from exercising its statutory investigatory and/or enforcement authority as set forth in the Election Campaign Control Ordinance, the Ethics Ordinance, and the Municipal Lobbying Ordinance should such allegations be contained in an Incident Report.
3. At the time of the call, in the instance where the complainant has identified him/herself, the third-party provider shall ask whether OEI may share his/her identity with persons outside of OEI. Identities of complainants will not be shared outside of OEI without such permission.
4. Intake and Review Committee reviews the complaint and determines whether it meets the criteria as set forth in Section VIII, B, Criteria for referral and resolution through OEI (i.e., allegations involving unethical conduct, fraud, waste and abuse). If the complaint meets the criteria, the Committee determines the appropriate City department for referral for investigation/resolution.
5. At the discretion of the OEI Deputy Chief or his/her designee, and based on the circumstances of the complaint, the

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complaint may be referred to the appropriate department for action prior to the Intake and Review Committee meeting.

6. If a complaint is received by OEI which contains allegations of misconduct or wrongdoing involving a member of the Intake and Review Committee, the member shall be informed a complaint has been filed. That member shall immediately recuse him/herself from the review of such complaint.
7. As follow-up, the OEI Deputy Chief or his/her designee may determine that an OEI staff member may need to obtain clarification or additional information from the complainant regarding the complaint/allegation.
8. OEI staff member prepares and forwards a memorandum and copy of the Incident Report to the appropriate department head, with within 2 business days of the Committee's review. The memorandum advises of the filing of the complaint, requests a response and advises of the process to secure additional information concerning the complaint, if necessary.
9. If the subject of the complaint is a supervisor/manager at any level, the complaint will be forwarded to and should be resolved by the next level of supervisor/manager. It is expected that the subject of the complaint will have no involvement in the response.
10. Complaints alleging criminal activity will be forwarded to the San Diego Police Department for investigation. Complaints against sworn officers may be forwarded to the Citizens Review Board of Police Practices for referral to Internal Affairs.
11. Complaints alleging improper financial activity and fraud, waste or abuse will be referred to the Auditor General for investigation.
12. If a complaint involves a department head, it is forwarded to the appropriate Deputy Chief for investigation/review.
13. Department Directors and any other personnel involved in the investigation of a complaint shall not share the substance of a complaint with anyone except those individuals who are directly involved in conducting the investigation. Such



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personnel provided with this information shall hold all information obtained as confidential to the greatest extent possible.

14. If it is deemed necessary by the Department/Division head to disclose the nature of the allegation(s) to the target for investigative purposes, such may be done by providing only a summary of the allegation(s). However, care should be taken to provide no information that would compromise the complainant's or any witness' identity. Sharing allegation(s) of non-compliance outside of the OEI intake process may constitute cause for an ethics complaint and/or for a legal claim of defamation.
15. Breaches of confidentiality may result in disciplinary action carried out through the existing process and procedures.
16. OEI staff member ensures, through monitoring and reminders to the affected Department head, that timely investigative and resolution activities are undertaken in response to complaints received through the hotline.
17. The OEI Deputy Chief or his/her designee in conjunction with the Intake and Review Committee will review the response submitted by the Division or Department head to determine if the allegation(s) raised in the complaint have been adequately addressed in the response. Upon such a determination, a memo from OEI to the Division or Department head will thereafter be provided, indicating closure of the matter.
18. However, if the response is deemed to inadequately address the allegation(s) raised in the complaint, the Division or Department head and appropriate Deputy Chief will be notified. The Division or Department head will be provided an opportunity to provide further clarification of the response and/or to further acquire additional information or to perform other actions as deemed necessary.
19. In the instance where a complainant has identified him/herself, such complainant will be notified of the OEI action on or referral of the complaint. The complainant may be advised that, in the instance of a referral, OEI may not be able to provide the complainant further information regarding the outcome of his/her complaint.

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### **III. Processing of All Other Employee Complaints**

1. OEI receives complaints by means other than through the Employee Hotline (e.g., e-mail, telephone, letter, etc.). Complainants may remain anonymous.
2. If the complaint is orally provided either in person or by telephone, an OEI staff member records, in writing, the factual allegation(s) of the complaint and attempts to obtain adequate information to facilitate an effective review.
3. OEI staff member logs the complaint and places a time/date stamp on all such complaints received.
4. OEI staff member enters the employee complaint into the third-party provider case management system.
5. Once entered into the case management system, the complaint is processed according to procedures as set forth in Section II, 2-14.

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#### **IV. Dissemination and Escalation Teams**

##### **Dissemination Team**

Upon completion of the call, the third-party provider sends Incident Reports to the City's designated dissemination team. The team consists of the following: (1) Deputy Chief Ethics and Integrity, (2) Ethics and Compliance Audit Specialist, and (3) Auditor General.<sup>1</sup>

A copy of all the incident reports will be forwarded to the Ethics Commission Director. He/she reviews each report to determine if there exist factual allegations suggesting a violation of any governmental ethics laws. Nothing contained in these policies and procedures shall preclude the Ethics Commission from exercising its statutory investigatory and/or enforcement authority as set forth in the Election Campaign Control Ordinance, the Ethics Ordinance, and the Municipal Lobbying Ordinance should such allegations be contained in an Incident Report.

##### **Escalation Team**

When a report is received that is designated for escalation (reports of high risk/threat situations requiring immediate notice), the third-party provider shall call the appropriate designated agency representatives immediately. The City has designated the Auditor General for financial emergencies, the Personnel Director for personnel-related matters, and the Labor Relations Manager for workplace violence. The notified representative will inform the Deputy Chief Ethics and Integrity of the call and respond as detailed in Section II, 2-14.

##### **Process**

##### **Standard Incident Report Dissemination**

Incident Reports shall be disseminated by the third-party provider, within two hours via email to the dissemination team members.

<sup>1</sup> The Auditor General position is subject to Council and Voter Approval. In the interim, we will use the existing process that is analogous to the City.

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### Escalation

If one of the following Incident Types is assigned to an Incident Report, and if it is determined the incident will happen again within 24 hours, then escalation is automatically triggered. Such Incident Types are:

- o Falsification of Organization Records
- o Fraud
- o Fraudulent Insurance Claims
- o Kickbacks
- o Improper Release of Proprietary Information
- o Substance Abuse
- o Theft of Cash
- o Theft of Goods/Services
- o Product Quality Concern
- o Workplace Violence/Threats

The third-party provider shall immediately call the appropriate designated escalation team representative if an Incident Report meets both of the following criteria:

Threat of or actual harm to employees, customers, or operations

Any significant incident projected to reoccur within 24 hours

All such reports are checked by the third-party provider's Quality Assurance Team prior to contacting the designated persons on the City's Escalation Team.

If the Deputy Chief Ethics and Integrity believes that any communication received by OEI or any OEI staff member constitutes a threat to any individual, organization, or to the public, he/she shall immediately notify the appropriate escalation team member and any other individual(s) as is deemed appropriate.

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## V. Processing of Citizen Complaints

1. OEI receives complaints of waste, fraud and abuse and/or other unethical conduct from citizens through a variety of means, including e-mail, telephone, letter, etc.
2. If the complaint is provided orally either in person or by telephone, an OEI staff member shall record, on a Citizens Complaint Form, the factual allegation(s) of the complaint and attempts to obtain adequate information to facilitate an effective review.
3. OEI staff member logs the complaint and places a time/date stamp on all such complaints received.
4. OEI staff member assigns a case number to each complaint to facilitate a follow-up process. As follow-up, the OEI staff member may need to clarify or obtain additional information regarding the complaint/allegation(s).
5. Once assigned a case number, the complaint is processed according to procedures as set forth in Section II, 2-14.
6. Employees, who are the subject of a complaint, shall be notified as set forth in the applicable MOU.

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## VI. Security for Complaints and Associated Reports, Working Papers, and Other Documents

### Policy

- All complaints, associated reports, working papers, and other documents detailing employee and citizen complaints, which are received either through the Employee Hotline, by mail, e-mail and those documents or notes of any oral conversations with City employees or citizens, shall remain confidential at all times.
- Such complaints, associated reports, working papers, and other documents shall **ONLY** be discussed with the Ethics Audit and Compliance Specialist, the Deputy Chief Ethics and Integrity and other individuals as determined by the Intake and Review Committee.
- No copies are to be made of any complaints, associated reports, working papers, and other documents, except for discussion in Intake and Review Committee meetings or when forwarded to a department head for investigation and resolution. At the conclusion of each Intake and Review Committee meeting all copies shall be destroyed and the original complaints, associated reports, working papers, and other documents shall be maintained in a secured manner by an OEI staff member as designated by the OEI Deputy Chief.
- Incident Reports and associated case numbers shall **ONLY** be provided to individuals who are responsible for conducting the investigation or reviewing of the complaint. Such information shall be held in strict confidence.
- The confidentiality of all complaints, associated reports, working papers, and other documents shall be maintained at all times by OEI and investigating/reviewing departments.
- Only the Deputy Chief Ethics and Integrity or his/her designee, in conjunction with the Office of City Attorney is authorized to determine the distribution or release of any complaints, associated reports, working papers, other documents and correspondence associated thereto, in accordance with the California Public Records Request Act (CPRA).

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#### Confidentiality

1. All complaints, associated reports, working papers, and other documents concerning the review or investigation of complaints shall be marked as **Confidential** documents by OEI and investigating/reviewing departments.
2. Strict confidentiality shall be maintained by OEI and investigating/reviewing departments throughout the processing of all complaints and through disposition/resolution and after.

#### Custodian Of Complaint Documents

OEI shall maintain custody of complaints, associated reports, working papers, and all other pertinent information regarding any investigations of complaints. Other parties involved in the investigation shall also retain their own documentation.

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## **VII. Requests for Information Regarding All Complaints**

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1. All requests for information concerning any employee or citizen complaint shall be directed for response to either the Ethics Audit and Compliance Specialist, the Assistant Deputy Chief Ethics and Integrity or the Deputy Chief Ethics and Integrity. The OEI shall respond to such requests as permissible under applicable state law and City policy, rules and regulations.
  2. Departments shall refer to OEI any CPRA or other requests for information regarding complaints received through OEI or the Employee Hotline.
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## VIII. Referral of Employee Complaints

### A. Background

#### Policy

City employees who have complaints or concerns regarding waste, fraud and abuse, individual or organizational processes, or who allege of non-compliance with City rules or regulations that relate to ethics, are encouraged to report such complaints or concerns to OEI. All such complaints and concerns shall be reviewed by the Intake and Review Committee for a determination of whether the allegation(s) are credible and appropriate for department referral through OEI.

### B. Methodology for Referral of Complaints

#### Procedures

- As complaints are received, the Ethics Audit and Compliance Specialist reviews and evaluates the seriousness of the allegation(s) to determine if the Intake and Review Committee should meet immediately.
- Otherwise, the Intake and Review Committee shall convene every two weeks to review the Incident Reports received by OEI and decide upon the referral of each report or any other appropriate action. A complaint may be referred to:
  - Deputy Chief
  - Department Director
  - Police Department
  - Auditor General
  - Ethics Commission
  - Citizens Review Board of Police Practices
  - Equal Employment Investigation Office
  - Other referral as deemed appropriate by the Committee
- OEI shall prepare a transmittal memo (refer to Section IX for examples) and attach a copy of the incident report.

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- The Ethics Audit and Compliance Specialist shall maintain a database that includes summary information from each complaint, assignment date, assigned to, meeting notes, memo sent date, forms sent date, received department response, and complaint matter is closed. This information is confidential and shall be securely maintained.

#### Criteria

An incident report shall contain all of the elements listed below to be within the purview of the Office of Ethics and Integrity, which will monitor the complaint until its disposition. The allegations contained in the report must be:

- **Credible** (Is worthy of belief in the opinion of the Intake Review Committee and appears to have been filed in good faith, with no malicious intent)
- **Ethics-Related** (Alleges waste, fraud, abuse or unethical behavior)
- **Timely** (Complaint should be filed within one year of the incident happening)

If the report does not address one or more of the above-mentioned issues, the report may be forwarded to the appropriate department director for their information and the Office of Ethics and Integrity will take no further action.

#### Referral to Auditor General

Any allegations of improper financial activity and fraud, waste and/or abuse will be referred to the Auditor General, who will determine the appropriate course of action.

The Auditor General should report to the Audit Committee the results of any investigation and disposition of such complaints. Documents reflecting such an investigation should be preserved in accordance with established procedures.<sup>1</sup>

The Auditor General will provide a copy of any investigation results and dispositions to OEI.

<sup>1</sup> Excerpt from the Kroll Report dated August 8, 2006, regarding the establishment of the Auditor General.

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## IX. Transmittal Memos

**Introduction** OEI uses the following types of transmittal memos to assign cases for investigation. A copy of the Incident Report is attached to the transmittal letter along with resolution forms. Identified or unidentified complainants receive memos or comments indicating the initial course of action by the Intake and Review Committee (e.g., referred to Deputy Chief for investigation).

### 1. Sample Memo when an Incident Report is Assigned to Department Director:

Date: October 30, 2006

To: Department Director

From: Jo Anne SawyerKnoll, Deputy Chief Ethics and Integrity

Subject: Employee Hotline Report <#>

Attached is a copy of a confidential incident report that was filed with the City's Employee Hotline. This office received the report on <date> regarding an issue or concern in your department. Since the report is specifically related to matters under your direction, you will best be able to address the issue(s) or concern(s) reported. Please ensure all existing policies and procedures are properly followed while reviewing or investigating this claim.

Callers are provided a report number and a date to call back to check the status of their complaint; additionally, it allows you to obtain any additional information that is needed as their allegations are investigated. For this reason, it is important that you respond to this report to provide feedback to the caller and to ensure that all issues or concerns are adequately addressed.

After you review the attached report, determine if you need any additional information from the caller and provide the caller with a status report (even if no action is to be taken). To do so, send an email with all questions and/or comments to The Network, our independent third-party hotline provider, at [NetworkCallbacks@tnwinc.com](mailto:NetworkCallbacks@tnwinc.com) and copy the [DeputyChiefEthicsIntegrity@sanidiego.gov](mailto:DeputyChiefEthicsIntegrity@sanidiego.gov). When submitting your questions and/or comments, include the report number, as indicated on the attached report, in the subject line by the response date provided in the *Client Instructions* section of the report. Your questions and/or comments will be forwarded to the caller should they call back on or after their assigned date.

In order to help sustain the integrity and success of the hotline, send the attached forms completed and signed to Danielle Knighten, MS 9A, within 10 business days of receiving this memo. If you have any additional questions regarding the incident report, or this process, contact Danielle at (619) 236-7072. We want to ensure all issues or concerns are addressed in a timely manner.

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2. Sample Memo when Incident Report is provided to Department Director for informational purposes only:

Date: October 30, 2006  
 To: Department Director  
 From: Jo Anne SawyerKnoll, Deputy Chief Ethics and Integrity  
 Subject: Employee Hotline Report <#>

Attached is a copy of a confidential incident report that was filed with the City's Employee Hotline. This office received the report on <date> regarding a complaint/issue or concern in your department. The Intake and Review Committee has established a process for screening the complaints/concerns and it has been determined that this complaint/concern does not require further action be taken by OEI; however, we are providing this report to you for informational purposes. You do not need to provide a response regarding this report.

Accordingly, if you feel that an investigation is necessary, ensure all existing policies and procedures are properly followed while reviewing or investigating this claim and contact us to discuss any action you plan to take, so we can update our records as needed. If you have any questions regarding this report or this process, you can contact Danielle Knighten at (619) 236-7072.

Thank you.

3. Sample Memo to an identified caller whose complaint meets the criteria set forth in Section VIII, B, Criteria:

Date: October 30, 2006  
 To: Identified Caller  
 From: Jo Anne SawyerKnoll, Deputy Chief Ethics and Integrity  
 Subject: Employee Hotline Report <#> dated (...)

This office received your complaint/concern filed with the Employee Hotline and, upon an initial review, the Intake and Review Committee has determined that your concern should be referred to XXX for further review. Any further communications related to your concern should be directed to XXX. XXX has been instructed to provide a resolution to this office upon completion of his/her review or investigation.

The City of San Diego will not retaliate, nor will it tolerate retaliation against those who, in good faith, report suspected ethics violations or who participate in an investigation of suspected ethics violations. An act of retaliation should be reported immediately to the Office of Ethics and Integrity (OEI), which will investigate any such report as a potential ethics violation. In addition, those who bring matters to OEI are protected through the state Whistleblower Protection Act. Details of the Act can be found at <http://www.dir.ca.gov/dlse/whistleblowersnotice.doc>.

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If you feel your concern is not addressed, please contact this office directly via email at [deputychiefethics&integrity@sandiego.gov](mailto:deputychiefethics&integrity@sandiego.gov) and reference the report number above.

Due to the nature of the complaint filed, this office may not be able to provide you with the outcome.

We appreciate your efforts and thank you for "Doing the Right Thing!"

4. Sample Message sent to the unidentified caller indicating course of action taken by the Intake and Review Committee:

Your complaint/concern filed with this Hotline has been reviewed by the Intake and Review Committee and they have determined that your complaint/concern should be referred to XXX for further review. If you have additional information that would be useful in XXX's review into your complaint/concern please contact The Network again with any additional information.

If you feel your concern is not addressed, please contact this office directly via email at [deputychiefethics&integrity@sandiego.gov](mailto:deputychiefethics&integrity@sandiego.gov) and reference the report number above.

Due to the nature of the complaint filed, this office may not be able to provide you with the outcome.

We appreciate your efforts and thank you for "Doing the Right Thing!"

5. Sample memo requesting additional information from the identified complainant before the Intake and Review Committee proceeds because there is not enough information to make an informed decision:

Date: October 30, 2006  
 To: Caller  
 From: Jo Anne SawyerKnoll, Deputy Chief Ethics and Integrity  
 Subject: Complaint Filed

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All documents provided to this Office have been reviewed, but before this Office can move forward, please provide specific cases with appropriate details (e.g., etc). Your claim cannot be substantiated without the requested information. Once this information is provided, this Office will be able to determine the appropriate course of action.

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City Employee Hotline and Complaint Program	Effective Date 010/30/2006

6. Sample memo informing the identified complainant that his/her complaint does not meet the criteria as set forth in Section II 2-14, and therefore not in the purview of OEI:

Date: October 30, 2006  
 To: Identified Caller  
 From: Jo Anne SawyerKnoll, Deputy Chief Ethics and Integrity  
 Subject: Employee Hotline Report <#> dated (...)

This office received your complaint/concern filed with the Employee Hotline and, upon an initial review, the Intake and Review Committee has determined that this matter should be referred to XXX, (Title) Director for further review. We have determined that allegations contained in your complaint does not constitute an ethical violation and, therefore, is not within the purview of the Office of Ethics and Integrity. Accordingly, this office will not take any further action regarding this matter. Any further communications related to your concern should be directed to XXX. If you feel your concern is not addressed, you should then contact your union.

The City of San Diego will not retaliate, nor will it tolerate retaliation against those who, *in good faith*, report suspected ethics violations or who participate in an investigation of suspected ethics violations. An act of retaliation should be reported immediately to the Office of Ethics and Integrity (OEI), which will investigate any such report as a potential ethics violation. In addition, those who bring matters to OEI are protected through the state Whistleblower Protection Act. Details of the Act can be found at <http://www.dir.ca.gov/dlse/whistleblowersnotice.doc>.

We appreciate your efforts and thank you for "Doing the Right Thing!"

**What Are The Reporting Requirements?**

OEI requires a response within 10 days of receiving the memo.

**Extensions to Reporting Deadlines**

OEI will determine extensions on a case-by-case basis, but will generally grant extensions.

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7. Sample reminder memo to referred party that a response is due to OEI and the deadline is approaching:

Date: October 30, 2006  
 To: Department Directors  
 From: Jo Anne SawyerKnoll, Deputy Chief Ethics and Integrity  
 Subject: Hotline Report Response Deadline Reminder

You are receiving this memo as a reminder that your response(s) to the confidential hotline report(s) is(are) due by <date>. You have been asked to respond with 10 business days of receiving the memo dated <date>, and to date this office has not yet received your response. If you need details regarding the report(s) previously provided, please contact Danielle Knighten (619) 236-7072 or [dknighten@sanidiego.gov](mailto:dknighten@sanidiego.gov).

If you need more time to resolve the complaint, send an email to [deputychiefethicsintegrity@sanidiego.gov](mailto:deputychiefethicsintegrity@sanidiego.gov) explaining your course of action and why additional time is necessary to resolve the complaint properly. Otherwise, the resolution form(s) should be completed, signed and sent to Danielle at MS 9A, within 5 days of receiving this memo, unless other arrangements have been made. If you feel you have received this memo in error, contact Danielle to confirm your response has been received by OEI.

Your attention to this matter is greatly appreciated.

8. Sample memo to referred parties when a response is past due:

Date: October 30, 2006  
 To: Department Directors  
 From: Jo Anne SawyerKnoll, Deputy Chief Ethics and Integrity  
 Subject: Hotline Report Responses Outstanding

Within the last month, this office has forwarded one or more Hotline report(s) asking you to reply, and to date this office has not received your response. If you need details regarding the reports previously provided, contact Danielle Knighten at (619) 236-7072 or [dknighten@sanidiego.gov](mailto:dknighten@sanidiego.gov).

If you need more time to resolve the complaint, please contact Danielle or send an email to [deputychiefethicsintegrity@sanidiego.gov](mailto:deputychiefethicsintegrity@sanidiego.gov) explaining your course of action and why additional time is necessary to resolve the complaint properly. Otherwise, the outstanding resolution form(s) should be completed, signed and sent to Danielle, MS 9A within 5 days of receiving this memo, unless other arrangements have been made. If you feel you have received this memo in error, contact Danielle to confirm your response has been received by OEI.

Your attention to this matter is greatly appreciated.

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9. Sample memo to department directors or appropriate referred party when OEI closed the complaint:

Date: October 30, 2006  
 To: Department Directors  
 From: Jo Anne SawyerKnoll, Deputy Chief Ethics and Integrity  
 Subject: Employee Hotline Report <#>

On <date>, OEI received your response to the City's Employee Hotline report <#>. The Intake and Review Committee has reviewed the response and deems the response is satisfactory, therefore, OEI will close this case and no further action will be taken regarding this matter. If you have any questions regarding this report or the process, contact Danielle Knighten at (619) 236-7072.

We appreciate your contributions to improving the City's ethical climate and to making the hotline a success.



## City of San Diego

### Office of Ethics and Integrity

#### Addressing Submission of Suspected Wrongdoing (Whistleblowers)

A key defense against management override of internal controls is a process for anonymous submission of suspected wrongdoing (whistleblowing) that typically incorporates a telephone hotline. The issues posed below by the Association of Certified Fraud Examiners (ACFE) are some examples of questions to consider when designing an effective whistleblower hotline. While ACFE has stated that the questions are not intended to be all-inclusive, and that some items may not apply to every entity's operations, the Office of Ethics and Integrity addressed each area set forth by ACFE.

Whistleblower Issues for Audit Committees to Consider Tool	Yes	No	Partially	Comments
<b>A. Design Effectiveness</b>				
In assessing the design effectiveness of the hotline, a government audit committee should consider the following questions:				
1. Does the hotline have a dedicated hotline number, fax number, web site, e-mail address, and regular mail or post office box address to expedite reports of suspected incidents of misconduct?	X	<input type="checkbox"/>	<input type="checkbox"/>	The City of San Diego's Office of Ethics and Integrity (OEI) contracts with The Network for hotline administration, which includes a dedicated toll-free phone number. The Network has helped clients—including the ACFE-- collect information and address critical issues such as ethics and risk management for nearly 25 years. The Network has more than 2,200 clients, including 45% of the Fortune 500 and a large number of municipalities and government entities.

*Anonymous Submission of Suspected Wrongdoing (Whistleblowers)*

2. Does the hotline demonstrate confidentiality, including showing how caller ID, e-mail tracking, and other technologies cannot be used to identify the whistleblower? Has the government considered the use of an independent hotline operator to enhance the perception of confidentiality in addition to any real improvement?	X	<input type="checkbox"/>	<input type="checkbox"/>	The City of San Diego, through OEI, The Network in order to enhance the perception of confidentiality. Complaints made directly to OEI may also be made anonymously, and all complaints, associated reports, working papers, and other documents detailing employee and citizen complaints, shall remain confidential at all times
3. Does the hotline utilize trained interviewers to handle calls to the hotline rather than a voice mail system?	X	<input type="checkbox"/>	<input type="checkbox"/>	All calls to the hotline are handled by trained, third-party call takers who ask probative questions to gather necessary information. The hotline is staffed and available 24 hours/day, 365 days/year.
4. Is the hotline availability 24 hours a day, 365 days a year?	X	<input type="checkbox"/>	<input type="checkbox"/>	
5. Does the hotline have multilingual capability to support hotline callers with different ethnic backgrounds or those that are calling from different countries?	X	<input type="checkbox"/>	<input type="checkbox"/>	
6. Are callers provided with a unique identification number to enable them to call back later anonymously to receive feedback or follow-up questions from investigators?	X	<input type="checkbox"/>	<input type="checkbox"/>	Each caller is provided a unique identification number so that they can leave additional information (anonymously if they choose) and so OEI may inform them of the status of their concern (e.g., under investigation) or ask additional questions.
7. Does the government have a case management system to log all calls and their follow-up, to facilitate management of the resolution process, testing by internal auditors, and oversight by the audit committee?	X	<input type="checkbox"/>	<input type="checkbox"/>	The Network receives and records all hotline calls and then creates an "Incident Report." Incident Reports are tracked by OEI to facilitate management of the resolution process. The confidentiality of complaints and these reports is maintained at all times. Upon the establishment of the City of San Diego's Audit Committee, these procedures may be

				revised.
8. Has the government established protocols for the timely distribution of each type of complaint, regardless of the mechanism used to report the complaint? Are complaints of any kind involving senior management automatically and directly submitted to the audit committee without filtering by management or other government personnel?	X	<input type="checkbox"/>	<input type="checkbox"/>	Each complaint is reviewed by OEI's Intake and Review Committee (currently comprised of the Deputy Chief of Ethics and Integrity, Ethics and Audit Compliance Specialist, Director of Personnel and Auditor/Comptroller) within three weeks of its receipt. At the discretion of the OEI Deputy Chief or his/her designee, and based on the circumstances of the complaint, the complaint may be referred to the appropriate department for action prior to the Intake and Review Committee meeting. In the absence of the Audit Committee, complaints involving senior management are referred within existing City mechanisms (e.g., EEIO, Police Department, etc.), depending on the nature of the allegation(s).
9. Does the government effectively distribute comprehensive educational materials and training programs among potential users to raise awareness of the hotline? Are these materials available in all relevant languages, given the potential user base and taking into consideration cultural differences that may require alternative approaches to achieve the desired goal?	<input type="checkbox"/>	<input type="checkbox"/>	X	In November-December 2005, literature, wallet cards, and flyers with information on the hotline (what it is, how to contact, etc.) were sent to <i>all</i> City employees.  OEI is currently participating in meet and confer with the City's unions to finalize the hotline procedures. Upon completion of this process, OEI and the Internal Communications group will undertake a City-wide education program to familiarize employees with the hotline, criteria for calls, process for handling concerns, etc. In the meantime, OEI is making in-person presentations to employees that describe the hotline (thus far reaching an estimated 1/3 of the City's workforce) and information is available on OEI's intranet and

<p>10. Does the government support outreach to potential stakeholders other than employees?</p>	<input type="checkbox"/>	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<p>Internet sites. At this point in time, the hotline is intended for employees only. Complaints from citizens are accepted through other means (phone calls, e-mails, in-person, etc.), but addressed through an analogous process. Upon formation of the Audit Committee, the hotline may be expanded to receive citizen complaints, also. At that point, OEI will reach out to citizens and other potential stakeholders.</p>
<p>11. Do the government's internal auditors periodically evaluate the design and operating effectiveness of the hotline? What were the internal auditors' conclusions regarding how the hotline reflects changes in the government's operations and in best practices; (2) whether the hotline is receiving satisfactory support from management, employees, and other participants; and, (3) whether protocols established for forwarding information to the government audit committee have been followed?</p>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<p>The City's Auditor/Comptroller is part of the hotline process and was involved in designing the process for effectively operating the hotline and processing complaints. The Deputy Chief of Ethics and Integrity is instrumental informing City management and ensuring appropriate support from management. The Ethics Audit and Compliance Specialist is responsible for advising the Intake and Review Committee on protocol issues.</p>
<p><b>B. Educating Employees and Others About the Hotline</b></p>				
<p>In assessing whether management is actively promoting the existence and use of the hotline, a government audit committee should consider the following questions:</p>				
<p>1. Is confidentiality of communications made to the hotline stressed?</p>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<p>All complaints, associated reports, working papers, and other documents detailing employee and citizen complaints, which are received either through the Employee Hotline, by mail, e-mail and those documents or notes of any oral conversations with City employees</p>

				or citizens, shall remain confidential at all times, as described in OEI procedures.
2. Is training provided to employees upon hiring and periodically thereafter?	<input type="checkbox"/>	<input type="checkbox"/>	X	OEI will begin its ethics training, slated to include information on the hotline and other mechanisms for reporting complaints involving waste, fraud, abuse or other unethical behavior, in early 2007. In the meantime, all new employees receive information regarding the employee hotline upon hire. Current employees may contact OEI at any time for information regarding or assistance with the hotline or ethics-related questions. Information on how to do so is available on the intranet and Internet, and through in-person presentations.
3. For suppliers, is information incorporated into a vendor approval process, in purchase contracts, and on purchase orders?	<input type="checkbox"/>	X	<input type="checkbox"/>	By Spring 2007, to accompany a Contractor's Code of Conduct, a brochure with information about the ethics-related rules and regulations that govern City employee behavior will be provided to firms doing business with the City. This will assist contractors in avoiding behavior that may encourage ethical lapses and will include information about how contractors can report ethical lapses to the City.
4. Is the hotline number and other contact information provided on the government's Web site, intranet, newsletters, invoices, purchase orders, pay stubs, checks, and even vehicles?	<input type="checkbox"/>	<input type="checkbox"/>	X	As the hotline is currently intended only for employees, the hotline number and contact information is made available through OEI's intranet site, in-person presentations, and collateral such as bookmarks. Upon formation of the Audit Committee, the hotline may be expanded to receive citizen complaints, also. At that point, OEI will reach out to citizens and other potential stakeholders through a variety of means.
<b>C. Evaluating Communications Received</b>				

In evaluating the communications received, a government audit committee should consider the following questions:				
1. Is management taking all communications made to the hotline seriously? Are allegations appropriately investigated?	X	<input type="checkbox"/>	<input type="checkbox"/>	The OEI Deputy Chief or his/her designee, in conjunction with the Intake and Review Committee, reviews each investigations' response to determine if the allegation(s) raised in the complaint have been adequately addressed in the response. If the response is deemed to inadequately address the allegation(s) raised in the complaint, the Division or Department head and appropriate Deputy Chief are notified. This allows OEI to verify appropriate investigation of complaints while assessing management support.
2. Does the government have a process for reporting back to the whistleblower on a timely basis, where possible, regarding the action taken?	X			In the instance where a complainant has identified him/herself, such complainant will be notified of the OEI action on or referral of the complaint. The complainant may be advised that, in the instance of a referral, OEI may not be able to provide the complainant further information regarding the outcome of his/her complaint due to confidentiality or personnel-related issues. For an anonymous complainant, a notification is sent to The Network so when the complainant calls back, he/she will know the disposition of the complaint and will have an opportunity to report additional information.

**City of San Diego  
Kroll Remediation  
Remedial Category – Interest Allocation**

Kroll Item	Report Ref.	Description
74	M-16	The interest allocation process should receive sufficient management review.

**Background**

During its audit, KPMG discovered that the interest accrual was allocated incorrectly. Current City management believes this was caused by either an accountant key punch error or a manual calculation error. Current City management believes this issue will be remediated by November 2006. Documented controls currently in place should prevent this type of error from happening again.

**Action Taken for Kroll Remediation**

The interest allocation process was documented in a format that management believes is acceptable for internal controls. The documentation includes:

- Process flow, process narrative and identification of significant control activities
- Control matrix containing:
  - Control objectives, risks, significant control activities, control number, control type
  - Identification of preventive/detective control, system or manual control, control frequency, fraud control, safeguarding of assets, financial statement assertions and the pertinent components of internal control from the COSO (Committee of Sponsoring Organizations of the Treadway Commission) framework

**Design Effectiveness Assessment**

Effective with the exception of one Design Gap - Segregation of duties related to significant control activity 74D. The same accountant has AMRIS (general ledger) system access to run preliminary and final reports. Management is in the process of remediating this gap by having information technology change system access. Once this gap is fixed, the accountant that runs the preliminary report will not be able to run the final report. This gap is planned to be remediated prior to the time that interest allocation is performed for November 2006.

**Operating Effectiveness Assessment**

Management plans to test operating effectiveness by March 31, 2007.

**Process Improvement Recommendations**

None.

# Kroll Remediation Item 74

## Interest Allocation Process

Control Objective	Risks	Significant Control Activity	CA	Ctrl Type						F/S Assertions					COSO				
			Ref		P/D	S/M	F	FC	SOA	Comp	E/O	V/A	R/O	P/D	C	R	I	M	E
Interest income is allocated to the appropriate funds for financial reporting	Interest income is not properly allocated to the appropriate funds resulting in inaccurate financial reporting	Accountant reconciles cash interest earned and investment balances among SunGard Investment Reports and AMRIS.	74A	R	P	M	M					X		X	X				
		AMRIS system allocates interest among investment pool accounts.	74B	C	P	S	SY					X		X	X	X			
		The preliminary report and supporting data are reviewed and approved by the Operations Section Supervisor.	74C	M	P	M	M					X		X	X			X	
		The Accountant has system access to run preliminary reports. The Supervisor has system access to run the final reports. THIS IS CURRENTLY A GAP AND SYSTEM ACCESS NEEDS TO BE ADDRESSED.	74D	SD	P	S	SY									X			

### Reference Legend

#### Control Type

A - Authorization  
 C - Configuration/account mapping  
 E - Exception reports/edit checks  
 I - Interface/conversion controls  
 K - Key performance indicators  
 M - Management review  
 R - Reconciliation  
 SD - Segregation of duties  
 SA - System access  
 SOA - Safeguarding of Assets

#### (F) Frequency

D - Daily  
 W - Weekly  
 B - Bi-Weekly  
 M - Monthly  
 Q - Quarterly  
 S - Semi Annual  
 A - Annually  
 T - Transactional - daily  
 SY - System

#### F/S Assertions

Comp - Completeness  
 E/O - Existence or occurrence  
 V/A - Valuation or allocation  
 R/O - Rights and obligations  
 P/D - Presentation and disclosure

#### COSO Framework

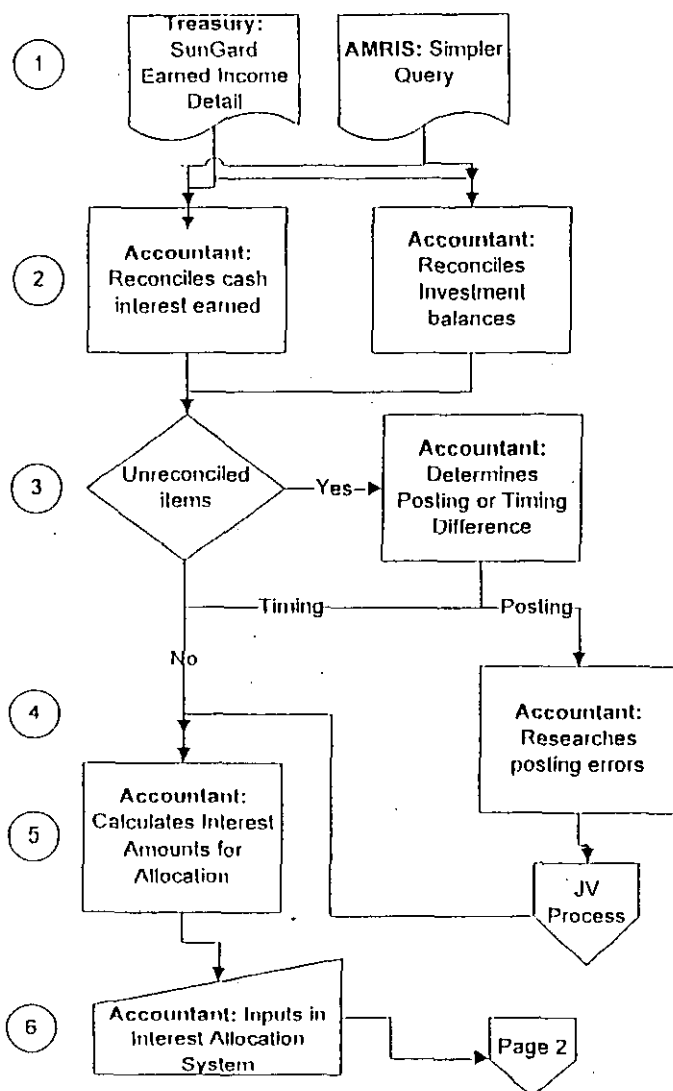
C - Control Activities  
 R - Risk Assessment  
 I - Information and Communications  
 M - Monitoring  
 E - Control Environment

#### Headers

CA Ref - Control Activity reference number  
 Ctrl Type - Control Type  
 P/D - Preventive/Detective Control  
 S/M - System/Manual Control  
 F - Frequency  
 FC - Fraud Control  
 SOA - Safeguarding of Assets



## Process Flow



## Process Narrative

Background: Interest is required to be allocated to all funds included in the City's pooled cash. Fund 99998 is the City's investment pool account. There are approximately 1,500 funds in the pool. Interest allocation distribution occurs on a calendar month basis. The City's AMRIS accounting system is on a 13 period basis. Interest Allocation Procedures were issued on 8/23/1999. That document serves as a "Desk Procedure."

The process begins with the receipt of the SunGard Monthly Investment Reports from the Treasurer's Department. These reports are available 2-3 weeks after month end. The SunGard report amounts need to be reconciled to the amounts in AMRIS. The Interest Allocation Accountant runs a Simpler query to obtain AMRIS fund amounts.

The Interest Allocation Accountant reconciles cash interest earned between the SunGard Investment Report and AMRIS. The Interest Allocation Accountant also reconciles investment balances among SunGard and AMRIS. Cash interest received and investment pool activity must reconcile prior to allocating interest to the funds.

There could be unreconciled items due to timing or posting errors. When there are unreconciled items, first the Interest Allocation Accountant researches for any timing differences. Typically, timing differences are related to posting on the first day of the next calendar month in AMRIS. A query report from the Simpler system is run to obtain daily transactions for the first day of the next calendar month. This report is used to identify timing differences.

If there are posting errors, they are researched with the supervisor and a Journal Voucher is prepared.

Upon completion of the reconciliation, the "TOTAL ENDING ACCRUAL" and "TOTAL CASH RECEIVED" is calculated by the Interest Allocation Accountant. Both figures are calculated from data contained in the SunGard Monthly Investment Reports.

Once these amounts are determined, they are entered into the Interest Allocation System (C3502 screen) with a status of "P" for Preliminary.

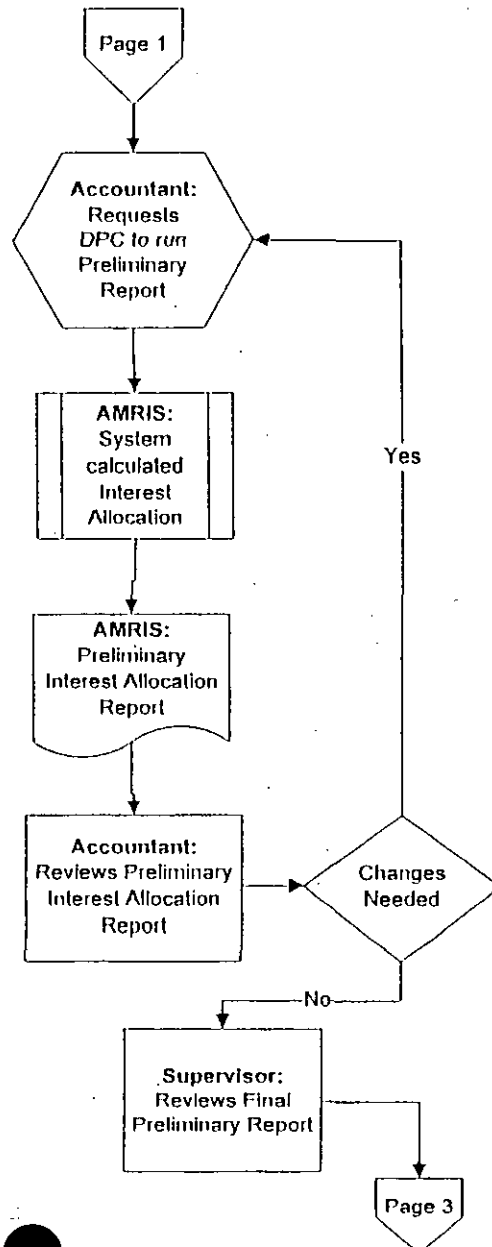
## Significant Control Activities

- 2 (CA - 74A) Reconciliation. Accountant reconciles cash interest earned and investment balances among SunGard Investment Reports and AMRIS.

## Process Flow

## Process Narrative

## Significant Control Activities



The Interest Allocation Accountant requests the preliminary interest allocation reports be printed. The accountant sends an email to San Diego Data Processing Corporation (DPC) indicating jobs needed to run the preliminary report.

DPC runs AMRIS system preliminary reports that show the results of interest allocation distribution based on the two amounts entered for the TOTAL ENDING ACCRUAL AND TOTAL CASH RECEIVED.

The Interest Allocation Accountant reviews the preliminary report. Specifically, the ending accrual, beginning accrual and cash received amounts are reviewed to confirm they are accurate. Three particular funds are analyzed for reasonableness: General Fund (100), Water Fund (41500), and Sewer Fund (41506). These three funds were chosen because each have substantial cash balances. The prior monthly reports for these three funds are compared to the current reports for reasonableness. At this time, the Interest Allocation Accountant can also enter any needed adjustments to cash or accrual balances into the Interest Allocation System. These adjustments are based on information from the preliminary report. If any adjustments are made, another preliminary report run is run and reviewed for accuracy.

After complete review of the preliminary report and any adjustments, the Interest Allocation Accountant submits all documents and work papers to the Operations Section Supervisor. The Operations Section Supervisor reviews the summary and supporting information and approves by initialing the front page of the work papers.

8

(CA - 74B) System Configuration. AMRIS system allocates interest among investment pool accounts.

11

(CA - 74C) Management Review. The preliminary report and supporting data are reviewed and approved by the Operations Section Supervisor.

## Process Flow

## Process Narrative

Significant Control  
Activities

Page 2

12 Supervisor: Modifies  
AMRIS status to Final

With the Operations Section Supervisor's approval, the posting of Interest Allocation is ready. The Supervisor modifies the status of the C3502 screen to "F" for Final.

13 Accountant:  
Requests  
DPC to run  
Final Report

The Interest Allocation Accountant sends an email to San Diego DPC indicating jobs needed to run the Final Interest Allocation Report and the system generated postings to AMRIS (the G/L).

14 AMRIS:  
System  
calculated  
Interest  
Allocation

DPC runs AMRIS system generated Final Interest Allocation Reports.

AMRIS: Final  
Interest Allocation  
Report

15 Accountant:  
Verifies AMRIS  
has posted

The Interest Allocation Accountant reviews the final report and verifies that AMRIS has posted interest allocation.

16 Accountant:  
Provides  
data to  
Treasury

The Interest Allocation Accountant provides receiving fund daily average cash balances to the Treasurer's Department through email. The work papers for the month are filed in the Interest Allocation file.

17 Accountant:  
Files work  
papers

End

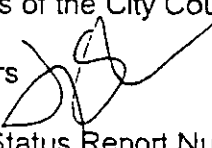
12 (CA - 74D) Segregation of Duties. The Accountant has system access to run preliminary reports. The Supervisor has system access to run the final reports. THIS IS CURRENTLY A GAP AND SYSTEM ACCESS NEEDS TO BE ADDRESSED.

14 See CA - 74B on page 2 of 3.



**OFFICE OF MAYOR JERRY SANDERS  
CITY OF SAN DIEGO**

**MEMORANDUM**

Date: November 22, 2006  
To: Honorable Members of the City Council  
From: Mayor Jerry Sanders   
Subject: Kroll Remediation Status Report Number 3, prepared for  
December 6, 2006, Council Meeting

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In my memorandum dated August 24, 2006, I reported my staff had identified 121 items for remediation from the Kroll Report. These items were grouped by remedial category and were described in detail along with anticipated due dates. I have already issued two memorandums on status (dated October 5, 2006, and October 30, 2006). This is my third memorandum regarding status of the City's Kroll remediation efforts. On December 6, 2006, my staff will meet with you to discuss the following:

- Status of remedial items completed as of December 6, 2006
- Status of remedial items in-process as of December 6, 2006

Cc: City Attorney  
Chief Operating Officer  
Chief Financial Officer  
Independent Budget Analyst  
SDCERS  
John Dyer

## I. Remedial Items Completed

### A. Items Previously Reported Complete

Kroll Item #	Kroll Category	Memorandum Reference
7-12	Organizational Structure	October 5, 2006
24	Audit Committee – Formation and Duties	October 30, 2006
45	Budget Policies and Practices	October 30, 2006
46-47	City Actuarial Services	October 5, 2006
48(i)	Deferred Maintenance	October 5, 2006
54-57	Financial Reporting	October 30, 2006
57.1	Financial Reporting	October 5, 2006
74	Interest Allocation	October 30, 2006
84-85	Reconciliation of Accounts	October 30, 2006
107.1	City Funding of SDCERS	October 5, 2006

### B. Items Completed During this Reporting Period

#### Remedial Category – Disclosure

49. Continue the operations of the Disclosure Practices Working Group (DPWG) and add the CFO not only as an official member but also have this person serve as chair. (Pages 249, M-4 & M-5)

**Status:** Mayoral task complete. The Mayor's Office submitted a Request for Council Action that the City Council direct the City Attorney to amend the Municipal Code<sup>1</sup> for the following changes to the DPWG.

- The Chief Financial Officer will serve as the chair of the revised DPWG.
- Membership in the DPWG will consists of the following five official voting members: Chief Operating Officer, Chief Financial Officer, City Attorney, Auditor General and Independent Budget Analyst (or designees). Outside disclosure counsel serves as an ex-officio member.
- No DPWG committee member (including the Chair) can prevent any other committee member from placing an item on the agenda.

#### Remedial Category – Forecasting/Projections

66. The CFO and Mayor should submit annually to the City Council as part of the annual budgeting process, a rolling five-year proposed plan that contains major items, including capital expenditures, deferred maintenance, debt payments and

<sup>1</sup> San Diego Municipal Code, Chapter 2: Government, Article 2, Administrative Code, Division 41: Securities Disclosure

## **II. Remedial Items Completed**

other major contractual obligations, major revenues by category and a forecast of gross cash receipts and gross cash expenditures. (Pages 262 & M-13)

**Status:** Complete. The Mayor announced the City's first five-year financial plan on November 14, 2006. The plan will be presented to the City Council on November 29, 2006. The plan addresses major items, including capital expenditures, deferred maintenance, debt payments and other major contractual obligations, major revenues by category and a forecast of gross cash receipts and gross cash expenditures. The plan can be accessed on the City's website at:

[http://www.sandiego.gov/mayor/pdf/five\\_year\\_plan\\_11\\_15.pdf](http://www.sandiego.gov/mayor/pdf/five_year_plan_11_15.pdf)

### **Remedial Category – City Funding of SDCERS**

107. The City and SDCERS should make a voluntary disclosure through a self-reporting process to the IRS of the amount of any improper diversion of funds used to pay retiree health care benefits and cooperate with the IRS to bring the City's retiree healthcare funding into full compliance. (Pages 259 & M-11)

**Status:** Complete. SDCERS tax consultant, Ice Miller LLP, filed a Voluntary Correction Plan report titled "Exclusive Benefit and Prohibited Transactions – Retiree Medical Benefits (401(h) Account)" with the Internal Revenue Service on June 22, 2006.

108. The costs should be reflected in the City's annual budget and five-year plan, and variances caused by changes in actuarial assumptions should be explained. (Page 260)

**Status:** Complete. For clarification purposes, Kroll item 108 relates to costs for proposed new retirement benefits for city employees.

The City acknowledges the need to accurately calculate the costs of any new retirement benefits and includes such costs in all budgets and five-year plans. Additionally, the voters passed Proposition B which will require the City to obtain voter approval for any increases (with the exception of cost-of-living) in municipal pension benefits.

## II. Remedial Items In-Process

### A. Items In-Process Previously Reported

Kroll Item #	Kroll Category	Memorandum Reference	Updated status?
1-6	Oversight Monitor	October 5 and 30, 2006	Yes *
13-14	Organizational Structure	October 5, 2006	No
18-23	Audit Committee, Formation and Duties	October 30, 2006	No
42	Ethics	October 30, 2006	Yes *
43-44	Budget Policies and Practices	October 30, 2006	No
86	Reconciliation of Accounts	October 5, 2006	No
87	Retirement Benefits	October 30, 2006	Yes *

\* see below

#### **Remedial Category - Oversight Monitor**

1. Appoint a Monitor to oversee the implementation of and compliance with the Remediation Plan. (Pages 263 & M-14)
2. The Monitor should be selected by the Mayor in consultation with the City Council and subject to the approval of the SEC and should be an independent person of suitable standing, independence and experience for the assignment. (Pages 263 & M-14)
3. The Monitor should have complete and unfettered access to all City and SDCERS personnel and records. (Pages 263 & M-14)
4. The Monitor should make quarterly reports to the City and the SEC on the City's progress. (Pages 263 & M-14)
- 4.1 City Monitor quarterly reports should be made public in an appropriate manner including on the City's website. (Page M-14)
5. The Monitor should serve a term of no less than three years and should be provided adequate resources to carry the duties of his office. (Pages 263 & M-14)
6. The SEC should have the right, upon request, to expand the scope of the Monitor's duties following consultation with the City. (Pages 263 & M-14)

#### **Updated Status:**

In process. The Kroll Report recommended an independent monitor oversee implementation of and compliance with the Remediation Plan. The City's settlement with the Security and Exchange Commission (SEC) requires that an independent consultant/monitor be hired within 60 days from the November 14, 2006, settlement date. The City believes that the independent consultant function called for by the SEC and the monitor role recommended in the Kroll Report can be reconciled and performed by the same person.

## Remedial Category – Ethics

42. To discourage any improper influence of the professionals who serve as "gatekeepers" to the public financial reporting process of the City, the Municipal Code should be amended to add criminal penalties for such conduct. It should be unlawful for any elected official, or employee of the City, or anyone acting under their direction, to take any action to corruptly influence, coerce, manipulate or mislead any independent certified public accountant engaged in the performance of an audit of the financial statements of the City or its component units, or outside legal counsel performing services for the City in connection with an offering statement of the City, or any actuary performing an actuarial valuation in connection with the preparation of the City's or SDCERS's CAFRs, or employees of a bond rating agency performing a credit rating of the City's bonds. (Page M-6)

**Updated Status:** City Attorney action complete. The City Attorney prepared an ordinance and submitted it for City Council Action on November 1, 2006. On November 13, 2006, at the Special City Council Financial Hearing, the ordinance was referred to the Rules Committee. The Rules Committee is tentatively scheduled to review the ordinance at its scheduled meeting on January 10, 2007.

## Remedial Category – Retirement Benefits

87. The City Council and employees should develop realistic retirement plan parameters for future City hires. This includes positioning the City to attract and retain the talent needed to meet the citizens' expectations for services, not be viewed as providing excessive benefit levels, and creating a plan the City can afford. (Page M-25)

**Updated Status:** The following three evaluations are in process and should be complete by December 29, 2006:

- Actuarial evaluations of the cost implications of formula changes to the existing retirement systems
- Benchmark study of Police Compensation and benefits for all employees
- Benchmark study of Fire Compensation and benefits for all employees



## II. Remedial Items In-Process

### B. Items In-Process During this Reporting Period

There are over 120 Kroll remediation items that span many categories, departments and related entities. My staff continues to coordinate with the responsible parties related to Kroll remediation status and milestone dates.

Additionally, for Kroll remediation items that can be executed by accounting/finance staff, Jay Goldstone, Chief Financial Officer, has established a dedicated team which has kicked-off remediation planning, scoping and action for the following Kroll items.

Kroll Item #	Kroll Category
58-59, 64-65	Financial Reporting
75-80 *	Internal Controls
81.	Personnel
82	Procurement
83	Redevelopment Authority
86	Reconciliation of Accounts
88-89	Risk Management
90,95	Training

\* Kroll item 76 will require significant effort because it addresses remediation of internal control weaknesses identified in the Auditor and Comptroller's 2006 Annual Report on Internal Controls as well as Management Letters from the City's external auditors. As of November 22, 2006, my staff has identified approximately 35 additional financial internal control items that require remediation by June 30, 2007.

**CITY OF SAN DIEGO**

(FOR AUDITOR'S USE ONLY)

1. TO: Council President	2. FROM (ORIGINATING DEPARTMENT): Mayor Sanders	3. DATE: November 22, 2006
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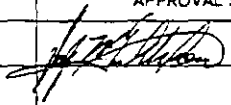
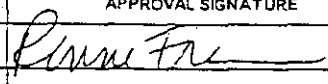
**Remediation Status Report Number 3 and Related Action**

4. PRIMARY CONTACT (NAME, PHONE & MAIL STA.): Way Goldstone / 236-5941	5. SECONDARY CONTACT (NAME, PHONE & MAIL STA.): John Dyer / 533-3978	7. CHECK BOX IF REPORT TO COUNCIL IS ATTACHED <input type="checkbox"/>
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**8. COMPLETE FOR ACCOUNTING PURPOSES**

FUND	DEPT.	ORGANIZATION	OBJECT ACCOUNT	JOB ORDER	C.I.P. NUMBER	AMOUNT	9. ADDITIONAL INFORMATION / ESTIMATED COST:

**10. ROUTING AND APPROVALS**

ROUTE (#)	APPROVING AUTHORITY	APPROVAL SIGNATURE	DATE SIGNED	ROUTE (#)	APPROVING AUTHORITY	APPROVAL SIGNATURE	DATE SIGNED
1	ORIGINATING DEPARTMENT		11/24/06	8	COO		11/22/06
2				9			
3				10			
4				11			
5							
6							

DOCKET COORD: \_\_\_\_\_ COUNCIL LIAISON: \_\_\_\_\_  
☒ COUNCIL PRESIDENT    ☐ SPOB    ☐ CONSENT    ☐ ADOPTION  
☐ REFER TO: \_\_\_\_\_ COUNCIL DATE: \_\_\_\_\_

ACTION OF:      ☒ RESOLUTION(S)      ☒ ORDINANCE(S)      ☐ AGREEMENT(S)      ☐ DEED(S)

Please docket the following for discussion at the special December 6, 2006 City Council meeting:

1. third informational update report on the Kroll remediation, and
2. directing the City Attorney to prepare an Ordinance amending the Municipal Code<sup>1</sup> consistent with the following changes:
  - The Chief Financial Officer will serve as the chair of the revised DPWG.
  - Membership in the DPWG will consists of the following five official voting members: Chief Operating Officer, Chief Financial Officer, City Attorney, Auditor General and Independent Budget Analyst (or designees). Outside disclosure counsel serves as an ex-officio member.
  - No DPWG committee member (including the Chair) can prevent any other committee member from placing an item on the agenda.

**11A. STAFF RECOMMENDATIONS:**

1. Docket the requested items for discussion
2. Approve the recommended action

**12. SPECIAL CONDITIONS:**

COUNCIL DISTRICT(S): ALL  
 COMMUNITY AREA(S):  
 ENVIRONMENTAL IMPACT:  
 HOUSING IMPACT:  
 OTHER ISSUES:

<sup>1</sup> San Diego Municipal Code, Chapter 2: Government, Article 2, Administrative Code, Division 41: Securities Disclosure



OFFICE OF MAYOR JERRY SANDERS  
CITY OF SAN DIEGO

MEMORANDUM

Date: April 9, 2007  
To: Honorable Members of the City Council  
From: Mayor Jerry Sanders *JPL*  
Subject: Kroll Remediation Status Report Number 5, prepared for  
April 23, 2007 Council Meeting

This is the fifth in a series of status reports regarding Kroll Remediation efforts. To date, approximately 62 or 51% of the 121 Kroll remediation items have been completed, or are substantially complete and more than 35 additional items are in-process. Although the City has made tremendous progress to date, there are still many important items remaining to complete our Kroll remediation efforts. On April 23, 2007 my staff will meet with you to discuss the following:

- Status of remedial items completed or substantially completed as of April 9, 2007
- Status of remedial items in-process as of April 9, 2007
- Timeline modifications

The status of all Kroll remediation items will continue to be provided to Mr. Stanley Keller, Independent Monitor, for observations and comments. Any conclusions made by him will be provided to the City Council.

Cc: City Attorney  
Chief Operating Officer  
Chief Financial Officer  
Stanley Keller, Independent Monitor  
Independent Budget Analyst  
SDCERS  
John Dyer

Attachment A - Greg Levin resume, comptroller functions  
Attachment B - Tracy McCraner resume, financial reporting functions  
Attachment C - Kyle Elser resume, internal audit functions

# I. Remedial Items Completed or Substantially Completed

## A. Items Previously Reported Completed or Substantially Completed

Kroll Item #	Kroll Category	Memo Reference	Additional Action Required		
			City Attorney	City Council	Mayor
1-6	Oversight Monitor	2/21/2007			
7-12	Organizational Structure	10/5/2006			
15	Staff Qualifications	2/21/2007			
18	Audit Committee – Formation and Duties (Long-Term Plan)	2/21/2007			Note A
19	Audit Committee – Formation and Duties (Eliminate FROB)	2/21/2007	Note B		
21	Audit Committee – Formation and Duties (Scheduled Meetings)	2/21/2007			
24	Audit Committee – Formation and Duties (whistleblower procedures)	10/30/2006		Note C	
42	Ethics	2/21/2007	Note D		
45	Budget Policies and Practices	10/30/2006			
46-47	City Actuarial Services	10/5/2006			
48(i)	Deferred Maintenance	10/5/2006			
49	Disclosure (DPWG)	11/22/2006		Note E	
51	Disclosure (City Attorney Confirmation)	2/21/2007			Note F
52	Disclosure (City Council Review Period)	2/21/2007			
53	Disclosure (DPWG and Audit Committee)	2/21/2007		Note E	
54-57	Financial Reporting	10/30/2006			
57.1	Financial Reporting	10/5/2006			
66	Forecasting/Projections	11/22/2006			
71	Information Technology – Financial Reporting Systems	2/21/2007			Note G
73	Information Technology – E-Mail Systems	2/21/2007			Note H
74	Interest Allocation	10/30/2006			Note F
82	Procurement	2/21/2007			Note F
84-85	Reconciliation of Accounts	10/30/2006			Note F
89	Risk Management	2/21/2007			
96	Training	2/21/2007		Note I	

Kroll Item #	Kroll Category	Memo Reference	Additional Action Required		
			City Attorney	City Council	Mayor
97	SDCERS Financial Reporting	2/21/2007			
98	SDCERS Internal Controls	2/21/2007			
99	SDCERS Actuarial Services	2/21/2007			
100-101	SDCERS Investment Advisors	2/21/2007			
103	City Funding of SDCERS	2/21/2007			
106	City Funding of SDCERS	2/21/2007		Note J	
107-108	City Funding of SDCERS	11/22/2006			
107.1	City Funding of SDCERS	10/5/2006			
113	SDCERS Organizational Structure	2/21/2007			
114	SDCERS Staff Qualifications	2/21/2007			
119,121	SDCERS Board Structure	2/21/2007			

Notes:

- A. Establishment of a Charter Review Committee; part of the committee's responsibilities include the long-term Audit Committee plan
- B. City Attorney to eliminate Financial Reporting Oversight Board (FROB) as redundant to the new Audit Committee
- C. Audit Committee to assume selected areas of responsibility for "whistleblower" policies and procedures
- D. Improper influence Ordinance was submitted to the City Council by the City Attorney on November 1, 2006; the City Council referred it to the Rules Committee on November 13, 2006; the Rules Committee chair has returned the Ordinance to the City Attorney for clarification
- E. City Council action required to direct the City Attorney to modify the Municipal Code to change the membership of the Disclosure Practices Working Group (DPWG) and have the DPWG report periodically to the Audit Committee
- F. Internal control operating design is complete; operating effectiveness (testing) to be performed or completed
- G. Short-term plan complete; long-term plan to be completed as part of Enterprise Resource Planning (ERP) project
- H. Short-term plan complete; long-term plan scheduled for completion by September 2007
- I. The Mayor's proposed budget for fiscal year 2008 contains adequate funding for training of personnel to ensure that they remain current on financial reporting standards; City Council action required to approve the budget
- J. An amendment repealing the "Waterfall" was introduced to the City Council on March 5, 2007; a second reading of the amended Ordinance is scheduled for April 10, 2007; however, a memo dated April 5, 2007 requested the City Attorney perform additional legal analysis prior to City Council action

# I. Remedial Items Completed or Substantially Completed

## B. Items Completed or Substantially Completed During this Reporting Period

Kroll Item #	Kroll Category	Memo Reference	Additional Action Required		
			City Attorney	City Council	Mayor
13-14 **	Organizational Structure (Comptroller and Director of Financial Reporting)	4/9/2007			
16-17	Organizational Structure (Staff Qualifications)	4/9/2007			
20	Audit Committee, Formation and Duties (written charter)	4/9/2007		Note K	
22	Audit Committee, Formation and Duties (audit requests)	4/9/2007		Note K	
23	Audit Committee, Formation and Duties (independent auditor retention)	4/9/2007		Note K	
104	City Funding of SDCERS	4/9/2007			
109-111	City Funding of SDCERS	4/9/2007			

\*\* Further action is required via a Charter Change

### Notes:

K. City Council action is required to approve the Audit Committee Charter

### **Remedial Category – Organizational Structure**

13. Establish the position of City Comptroller responsible for accounting and financial reporting, including preparation of the CAFRs and reporting to the CFO. (Pages 245, 246 & M-2)
14. Establish the position of Director of Financial Reporting responsible for the preparation of the City's periodic financial statements. (Pages 246 & M-2)

**Status:** Substantially complete. The City has assigned qualified personnel to serve in the capacity of Comptroller (Deputy Comptroller until the Charter is amended) and Director of Financial Reporting (refer to items 16 and 17 below for staff qualifications). City management believes the establishment of permanent position of Comptroller will require an amendment to the City Charter and perhaps the Municipal Code.

### **Remedial Category – Staff Qualifications**

16. The Comptroller should have significant experience in governmental accounting, including in the preparation of CAFRs in accordance with GASB and other applicable accounting and financial reporting standards, rules and regulations; should in particular be familiar with federal rules and regulations applicable to the

receipt of federal assistance and the issuance of public securities; and should also be competent to design, implement and operate an effective system of internal controls over financial reporting and disclosure. (Page M-2)

**Status:** Substantially complete (refer to item 13 above). The City has assigned Mr. Greg Levin the responsibilities of Deputy Comptroller. Mr. Levin has experience in government accounting, including the preparation of CAFRs in accordance with applicable accounting and financial reporting standards. He is familiar with federal rules and regulations applicable to the receipt of federal assistance and the issuance of public securities. Mr. Levin also has experience with internal controls over financial reporting and disclosure. See Attachment A for Mr. Levin's resume.

17. The Director of Financial Reporting would report to the Comptroller and would be responsible for the preparation of the City's periodic financial statements. This person should also have experience in the preparation of the CAFRs in accordance with GASB and other applicable accounting standards, rules and regulations. (Page M-2)

**Status:** Substantially complete (refer to item 14 above). The City has assigned Ms. Tracy McCraner the responsibilities of Director of Financial Reporting. This position reports to the Deputy Comptroller. Ms. McCraner has significant experience in government accounting, including the preparation of CAFRs in accordance with applicable accounting and financial reporting standards. See Attachment B for Ms. McCraner's resume.

#### **Remedial Category – Audit Committee, Formation and Duties**

20. The Audit Committee should establish a written charter. (Pages 251 & M-6)
22. The Mayor, CFO, City Attorney and City Council should have the authority to make requests of the Audit Committee and Auditor General (Internal Auditor) to perform internal audits of material matters they reasonably believe to be warranted. (Page 252)
23. With the assistance of the CFO and Auditor General (Internal Auditor), the City's independent auditors would be retained by, report to and take direction from the Audit Committee. (Page 252)

**Status:** Substantially complete via Audit Committee Charter. The Audit Committee approved a Charter, as well as Standing Rules for the Municipal Code and Mayor's Statement of Operating Principles and forwarded them to the City Council for consideration. City Council approval of these items is required.

Although the intent of items 22 and 23 above are addressed in the Audit Committee's Charter, the Charter does not fully address all Kroll requirements. For example the Audit Committee Charter does not state that the CFO can make requests of the Audit Committee and Internal Auditor to perform certain audits. Additionally, the Charter does not state that the CFO or Internal Auditor have input with the Audit Committee's selection of the City's independent auditors. The Charter states that the Mayor shall provide

## I. Remedial Items Completed or Substantially Completed

appropriate consultation with the Audit Committee's selection of the City's independent auditors.

### Remedial Category – City Funding of SDCERS

104. For purposes of calculating annual funding requirements, the UAAL should reflect a prudent view of economic reality and include within it the costs of the *Corbett* settlement. (Pages 259 & M-11)

**Status:** Substantially complete. SDCERS Board action approved and directed the actuary to include the costs of the *Corbett* settlement and 13th check. The Actuary report dated January 2007 contains these components in the UAAL. The Actuarial Valuation Report was presented at the SDCERS board meeting dated January 19, 2007. The link to the SDCERS board meeting agenda follows:

[http://www.sdcers.org/agendas/2007/january/bd\\_admin\\_1\\_19\\_07.pdf](http://www.sdcers.org/agendas/2007/january/bd_admin_1_19_07.pdf)  
(refer to page 6, item IV.A.1)

The January 2007 Actuarial Report can be accessed on SDCERS website at:

[http://www.sdcers.org/images/pdf/city\\_of\\_san\\_diego\\_actuarial\\_valuation\\_report\\_1\\_12\\_07\\_final.pdf](http://www.sdcers.org/images/pdf/city_of_san_diego_actuarial_valuation_report_1_12_07_final.pdf)  
(refer to pages 29 and 31)

In addition, the SDCERS Board has directed its actuary to complete an experience study which will be presented to the Board in the winter of 2008. This study will provide the Board with information to make further assumption decisions such as the appropriate discount rate and salary growth SDCERS should use.

109. The City, in response to the Report of the Pension Reform Committee, amended the Charter to require net actuarial losses be amortized over a period not longer than 15 years, net actuarial gains over a period not shorter than five years, and that SDCERS use an amortization period no greater than a fixed, straight-line five years for each new benefit improvement. It is recommended that the City use the same period for amortization of both gains and losses. (Pages 261 & M-12)
110. The plan's actuary should be engaged to develop a responsible funding program that considers expected cash distributions and the obligations to new and existing plan members. (Page M-25)
111. The Pension Reform Committee assessed the pension plans under funded status and offered recommendations related to reducing or eliminating the City's UAAL and reducing the ongoing annual costs related to the plan and contingent benefits. The City should re-evaluate the Committee's recommendations and, beyond those previously addressed in our Report, consider enacting those that are appropriate that do not conflict with our Remediation Plan. (Page M-18, M-19 & M-20)



Status: Complete. At its March 16, 2007 Board meeting, SDCERS adopted a 20 year amortization schedule to pay off the current UAAL. As part of the motion, the actuary was instructed to ensure that his calculation did not include any negative amortization. In addition, the SDCERS Board adopted a 15 year amortization schedule for all future gains or losses and a five year amortization schedule for any new pension benefits approved by the City. This will take effect for the June 30, 2007 actuarial valuation which will be reflected in the City's fiscal year 2009 budget.

The Mayor has included a supplemental pension payment in his proposed fiscal year 2008 budget to ensure no negative amortization and the beginning payoff of the existing UAAL.

## II. Remedial Items In-Process

### A. Items In-Process Previously Reported

Kroll Item #	Kroll Category	Memorandum Reference	Updated status?
43 ***	Budget Policies and Practices	February 21, 2007	Yes *
44	Budget Policies and Practices	October 30, 2006	No
52.1, 52.2	Disclosure	October 5, 2006	No
58-59	Financial Reporting	November 22, 2006	Yes **
64-65	Financial Reporting (accruals)	November 22, 2006	No
67	Information Technology, Financial Reporting Systems	February 21, 2007	Yes *
75-78	Internal Controls	November 22, 2006	No
79-80	Internal Controls	November 22, 2006	Yes **
81	Personnel	November 22, 2006	No
83	Redevelopment Authority	November 22, 2006	No
86	Reconciliation of Accounts	October 5, 2006	No
87	Retirement Benefits	October 30, 2006, November 22, 2006	No
88	Risk Management	November 22, 2006	No
90, 95	Training	November 22, 2006	No
102	SDCERS Financial Reporting	February 21, 2007	No
112	SDCERS Organizational Structure	February 21, 2007	No
120	SDCERS Board Structure	February 21, 2007	No

\* see below

\*\* see Section III

\*\*\* Item was previously reported as complete; however, based upon further review and discussions, item was moved back to in-process

#### **Remedial Category – Budget Policies and Practices**

43. In order to maintain current service levels and address issues such as deferred maintenance, the City must reduce expenditures by improving efficiency, increasing the current revenue base, and seeking alternative revenue sources. (Page M-14)

**Updated Status:** In-process. The Mayor's fiscal year 2008 takes the first significant steps towards reducing costs, improving efficiencies and funding the eight significant areas identified in the Five-year Financial Outlook, including deferred maintenance. While the fiscal year 2008 budget is balanced as proposed, and the funding gap in future years has been reduced, the City still has future budget challenges in order to meet its obligations and still provide current service levels.

The City's first five-year financial plan was presented to the Budget and Finance Committee on November 29, 2006. The plan addresses deferred maintenance, reducing expenditures via various methods, such as, elimination of positions; business process engineering and streamlining; employee benefit adjustments; debt refinancing; budget clean-up; release of encumbered funds; transfer of inactive fund

balances; establishing a property business improvement district; leveraging city assets and managed competition. Revenues are projected to increase through normal growth.

The Financial Outlook is only a tool to help produce a comprehensive, long-range analysis of the City's general fund revenues and expenditures. The five-year financial outlook will be regularly updated and will be used to assist with the preparation of the City's annual budget. The plan can be accessed on the City's website at:

[http://www.sandiego.gov/mayor/pdf/five\\_year\\_plan\\_11\\_15.pdf](http://www.sandiego.gov/mayor/pdf/five_year_plan_11_15.pdf)

#### **Remedial Category – Information Technology, Financial Reporting Systems**

67. By June 30, 2007, evaluate the information technology needs of the City, including benchmarking of existing systems against available systems suitable for management of the City's finances and the preparation of timely and accurate CAFRs and budgets. (Pages 247 & M-3)

**Updated Status:** In process. On January 5, 2007 San Diego Data Processing Corporation (SDDPC) issued a Request for Proposals (RFP) for the Enterprise Resource Planning (ERP) system software. Two qualified proposals were received by the proposal due date of February 9, 2007. The ERP System Evaluation and Selection Committee are expected to make a vendor recommendation to the ERP System Core Project Executive Steering Committee in the third week of April 2007. Following the selection of the software vendor, a RFP will be issued for a System Integrator. The System Integrator is expected to be selected in June 2007.

#### **B. Items In-Process During this Reporting Period**

##### **Remedial Category – Auditor General, Establishment and Responsibilities**

25. Create a new position of Auditor General (Internal Auditor) with responsibility for internal audits of the City's internal controls, financial accounting, reporting and disclosure; operations; and fraud, waste and abuse. This person would be nominated by the Mayor and confirmed by the majority of the City Council. (Pages 250 & M-5)
26. The new Auditor General (Internal Auditor) should report to the Audit Committee no less than on a quarterly basis and periodically to the City Council and should submit annually to the City Council a public report of his/her activities. (Pages 250 & M-5)
28. The Auditor General (Internal Auditor) should report to the Audit Committee the results of any investigation and disposition of such complaints. (Page 252)
29. In accordance with the *International Standards for the Professional Practice of Internal Auditing*, the Auditor General (Internal Auditor) should establish risk-based plans to determine the priorities of the internal audit activity. (Page M-17)

## II. Remedial Items In-Process

30. The City should require the Auditor General (Internal Auditor) to adopt a comprehensive risk assessment and planning process that actively addresses financial reporting, accounting activities, and other issues. (Page M-25)
31. The Auditor General (Internal Auditor) should use a systematic and disciplined approach based on a risk assessment to select audits. This risk assessment should be completed at least annually. The department should evaluate and contribute to improving risk management, controls, and governance processes. (Page M-17)
32. The department should base audit plans on both subjective analysis of comments from management and objective analysis of financial and operating data. (Page M-25)
34. Elected officials, their staff, and the City's senior management must be considered by the internal audit function. (Page M-17)

**Status:** In-process. The long-term plan for completion of the Internal Auditor Kroll remediation items will require a City Charter change. In the meantime, the City has implemented an interim solution. On March 26, 2007 the Mayor filled the position of Internal Auditor on an interim basis. This position will be staffed by Mr. Kyle Elser an existing City employee who has internal audit experience and qualifications. Refer to Attachment C for Mr. Elser's resume.

Additionally, the City has an open job announcement for an Internal Auditor to fill this position with an understanding that the reporting responsibilities of the Internal Audit position may change with City Charter amendments. The interim Internal Auditor will report to the Mayor and will meet with the City's Audit Committee no less than on a quarterly basis and periodically with the City Council as needed and will submit annually to the City Council a public report of his/her activities. Additionally, the Internal Auditor will present to the Audit Committee the results of any investigation and disposition of such complaints. Procedures will be established for reporting to the Audit Committee any information that is prohibited from public disclosure. During the interim period, the Internal Auditor will focus on performing a Citywide Risk Assessment in accordance with the *International Standards for the Professional Practice of Internal Auditing*, and develop audit plans based on the assessment. The assessment will include financial reporting and the City's internal controls over financial reporting.

### Remedial Category - Disclosure

50. The City should assign the responsibilities for preparing public documents and filings to the appropriate City employees. Ultimate responsibility for preparing these City documents cannot be assigned to the independent auditor, disclosure counsel, fiduciary counsel, actuary, or other professionals. (Page M-25)
60. City schedules requested by the external auditors should be prepared and internally reviewed before the auditors begin work. As part of a sound financial reporting system, the City should prepare supporting schedules and detail for all major accounts and transactions during the monthly closing process. (Page M-17)

61. The City should report as part of its annual CAFR staff's best estimate of material payments it will be required to make for each of the next five years and in aggregate thereafter, as a result of contractual commitments or other commitments the City reasonably intends to fulfill. This includes expected pension payments, retiree health premium payments, capital expenditures resulting from contractual commitments; material contractual commitments in excess of one year; deferred maintenance to extent qualified; and debt and lease obligations. (Page 254 & M-8)

**Status:** In-process. Interviews with process owners and documentation of internal controls are occurring.

#### **Remedial Category – Training**

91. MWWD employees should receive special training directed at ensuring the City complies with all contractual requirements, laws and regulations and reporting any noncompliance to the appropriate individuals or entities. (Pages 247 & M-2)
92. Tailored training for all individuals who are currently employed by the City who were members of the Metropolitan Wastewater Department at any time from 1995 to 2004, the period of the City's noncompliance with its SWRCB grant and loan covenants and its violation of the Federal Clean Water Act should also be developed. The Metropolitan Wastewater Department employees should receive special training directed at (i) ensuring the City complies with all contractual requirements, laws and regulations, and (ii) reporting any noncompliance to the appropriate individuals or entities. (Pages M-2 to M-3)
93. The City should educate the employees responsible for recording sewer invoices on how to identify the appropriate supporting documentation for Municipal and Metropolitan allocations in order to reduce the likelihood of significant misclassifications. (Page M-22 & M-23)

**Status:** In-process. Darlene Morrow-Truver, Deputy Director, MWWD, has initiated efforts on Kroll remediation for items 91-93 and is on schedule to complete the items by the established due date of July 2007.

94. Training of City staff and elected officials regarding their disclosure obligations under federal and state securities should be conducted no less frequently than every two years. (Pages 262 & M-13)

**Status:** In-process. Certain elected officials received disclosure training related to obligations under federal and state securities on March 5, 2007. The training was provided by outside consultant, John McNally of Hawkins Delafield & Wood LLP. In addition, on April 9, 2007, training will be provided by the City's independent auditors, specifically Jim Godsey of Macias Gini and O'Connell.

For City staff a two-part training session will be conducted by Mr. McNally on April 25 and 26, 2007. The session on April 25, 2007 is for Executive Team and Community & Legislative Services staff. The session on April 26, 2007 is in addition to the training on April 25, 2007. The Executive Team and Community & Legislative Services staff are required to attend both sessions. In addition, the April 26, 2007 training session is also for anyone in the

## II. Remedial Items In-Process

departments that directly or indirectly contribute to preparing or reviewing language that becomes part of the City's or an Agency's disclosure, with a particular focus on offering documents.

Appropriate policies and procedures are in the process of being amended to require that disclosure obligations training under federal and state securities be conducted no less frequently than every two years.

Kyle S. Elser, CPA, CIA

Work (619) 235-5805. Email: KElser@sandiego.gov

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### PROFESSIONAL EXPERIENCE

#### **City of San Diego**

*Payroll Manager (Principal Accountant)* Oct 2005 - Present

- ◆ Supervise eight staff members responsible for administering the City of San Diego's biweekly payroll, quarterly payroll tax returns and annual W-2 Forms.

*Internal Audit Supervisor (Principal Accountant)* Jan 2001 - Oct 2005

- ◆ Assisted in the development of the annual audit plan for the internal audit section.
- ◆ Supervised eight staff members in performing the internal audit plan.
- ◆ Reviewed workpapers and prepare audit reports for the Audit Division Manager's signature.
- ◆ Performed various audits and other projects while supervising internal audit section.

*Internal Auditor (Accountant II, Accountant III)* Aug 1996 - Jan 2001

- ◆ Performed internal audits to determine Departments' compliance with laws and regulations.
- ◆ Reviewed internal controls to ensure City assets were properly utilized and safeguarded.
- ◆ Made recommendations to correct internal control weaknesses identified.
- ◆ Performed contract compliance audits with the various City vendors and City agencies.
- ◆ Performed operational audits and made recommendations to increase process efficiencies.
- ◆ Performed audits to ensure City Departments were accurately reporting annual performance measures.

*External Revenue Auditor (Accountant Trainee, Accountant I)* Jan 1995 - Aug 1996

- ◆ Performed hotel tax, franchise tax, business license tax, and rental unit tax audits.

#### **Kornfeld & Levy, CPA's**

*Accountant* Feb 1988 - Jan 1995

- ◆ Performed professional accounting work preparing full disclosure financial statements.
- ◆ Prepared corporate, partnership, individual and payroll tax returns.

### EDUCATION

**Humboldt State University**

Graduated May 1987

B. S., Business Administration, Emphasis: Accounting  
Special Minor: Speech Communication

### CERTIFICATIONS

- ◆ Received Certified Public Accountant certification April 1999.
- ◆ Received Certified Internal Auditor certification May 1998.

1988-1995

City of San Diego-Auditor and Comptroller's Office  
Accountant

- Prepared the General Fund revenue and expenditure analysis.
- Responsible for the General Fund payments, Council Actions, Manager Actions and budget adjustments and year end financial statement preparation.
- Responsible for all Mayor and Council department analysis, data processing projections and special fund budgets.
- Responsible for all out of town travel and in town meetings expense review and monthly and quarterly reports to Council.

### EDUCATION

San Diego State University: Bachelor of Science Degree in Accounting

References available upon request.



- Responsible for the oversight and approval of the calculation of the City's departmental and federal overhead rates, and central service department billings to Enterprise funds for FY 2001 through 2006.
- Oversight of the transportation and park and recreation grant program.
- Oversight and review of the preparation of the Annual Streets, Tidelands and State Controller's Reports for fiscal years 2001, 2002 and 2003.

1999-2001

City of San Diego-Auditor and Comptroller's Office  
Accountant IV-Accounting Operations/CIP/Cost

- Managed 3-4 accountants and one account audit clerk. Reviewed all daily, monthly and year end work, financial statements and interim reports. Prepare staff performance plans and evaluations.
- Managed the compilation of the City's CAFR for fiscal year ending June 30, 1999. Coordinated weekly meetings with outside auditors, managed staff responsible for financials and footnote preparation.
- Responsible for the CIP budgets of all governmental projects city-wide, fund certification, project maintenance, capitalizations, etc.
- Responsible for first line review of the General Fund monthly revenue and expenditure analysis.
- Responsible for the Capital Projects and Debt Service sections of the CAFR for FY 2000 and 2001.
- Responsible for the City's blended component unit financial statements for the Facilities Equipment Leasing Corporation, Open Space Park Facilities District, Convention Center Corporation and Public Facilities Financing Authority.

1995-1999

City of San Diego-Auditor and Comptroller's Office  
Accountant III-CIP Cost Section

- Supervised 2 accountants and one account audit clerk, immediate supervision, daily hands on reviewer, provided input to performance evaluations to Accountant IV.
- Implementation team member for the new Fixed Asset Management System (FAMIS) and was responsible for overseeing the transition and reconciliation of all governmental asset data from the old fixed asset system to FAMIS.
- Responsible for the compilation of the General Fixed Asset Account Group (GFAAG) for CAFR's FY 1995-1999.
- Responsible for the Capital Outlay, Police Decentralization and bond funds for FY 1995-1999.
- Responsible for the buildings and improvements for all City of San Diego governmental projects, and related CIP budgets.
- Responsible for the special assessment debt funds for the City.

TRACY M MCCRANER  
(760)599- 0936 [tmccraner@sandiego.gov](mailto:tmccraner@sandiego.gov)

## OBJECTIVE

A senior management accounting position with a large governmental entity focusing on financial reporting and analysis

## PROFESSIONAL EXPERIENCE

2006 – present

City of San Diego-Auditor and Comptroller's Office  
Principal Accountant-CAFR/Accounting Operations

- Assigned as project manager to lead the CAFR team in the completion of the City's 2003 CAFR audit by KPMG, as well as the FY 2004 and 2005 CAFR audits with Macias Gini. Lead approximately 10 professional staff to ensure the completion of the City's 2003 annual report while also maintaining the continued progress of the City's 2004 and 2005 audits.
- Managed approximately 17 staff within the Accounting Operations and Accounts Payable sections of the Auditors office. This team was responsible for centralizing all payment review and approval processes city-wide, and successfully decreased payment turnaround times from a 5 day average to a 2 day average within 6 months of implementation.

2001-2006

City of San Diego-Auditor and Comptroller's Office  
Principal Accountant-Accounting Operations/CIP/Cost

- Managed 8-12 accountants and 4-7 account audit clerks. Reviewed daily, monthly and year end work, financial statements, interim statements, coordinated staff activities, and prepared annual and probationary performance evaluations.
- Responsible for the coordination and compilation of the City's Comprehensive Annual Financial Report (CAFR) for fiscal years (FY) ending June 30 2003, 2004 and 2005.
- GASB 34 implementation team member, ensured June 30, 2002 CAFR was in compliance with all GASB 34 requirements related to capitalization of infrastructure, depreciation on governmental assets, and long term liability adjustments to governmental debt. Was responsible for the hiring of outside consultant to assist in the valuation of all city-owned infrastructure and lead a team of City departments to ensure accurate reporting of all infrastructure assets.
- Supervised the preparation of the General Fund revenue and expenditure analysis, provided monthly reports to the City Manager/Mayor and City Council.
- Supervised the accountants in charge of General Fund, TOT, Emergency Medical Services, Public Liability, and Capital Improvements Program (CIP) budgets.

PO Box 125068  
San Diego, CA 92112

## Gregory Levin, CPA

Attachment A  
Cell: 619-793-0525

Korn/Ferry Futurestep, Sherman Oaks, CA

Project Analyst

6/1999-4/2001

- Implementing and Managing communications server and database of 700,000 candidates.
- Working as Community Events Manager (Discussion Boards and Chats).
- Performing quality assurance on corporate and client websites.
- Technical liaison between retention marketing group and IT department.

### Education

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Bachelor of Arts - Business Economics - Accounting

University of California at Santa Barbara

Coursework included Accounting, Monetary Economics, Personnel Economics and Finance.

### Certifications & Other Experience

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Certified Public Accountant, State of California License #90699

CPR certified

Outward Bound

Colorado School of Leadership and Survival Training

- 21-day wilderness leadership course

### Skills

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G/L accounting, Cost Accounting and Compliance Review, Financial Reporting Budget and GAAP, Microsoft Word, Excel, Access, Adobe Photoshop, Paint Shop Pro, Adobe Illustrator, Internet Proficient, MS Outlook Enterprise Email Software, Basic HTML, NT 4.0 Server Management

### Recent Training

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Completed continuing professional education in the following areas:

**Bisk:**

Internal Control and Fraud in Government Engagements 8/2006

**GFOA:**

GASB review 1/2006

Satellite Update 11/2004

Satellite Update 4/2004

**IIA:**

Sarbanes-Oxley: Process Improvement Workshop 8/2005

Sarbanes-Oxley Primer: Charting Your Course 6/2005

References and additional experience are available upon request

## Experience

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### City of San Diego Auditor & Comptroller, San Diego, CA

#### Financial Operations Manager

5/2006-Present

I am the Principal executive responsible for the operations of the Comptroller division of the Auditor & Comptroller's office. My responsibilities include accounts payable, comptroller systems, capital asset accounting, debt accounting, fund analysis, redevelopment accounting and financial reporting. During this time I have been responsible for direct oversight of the production of City's Comprehensive Annual Financial Report, including the successful completion of the City's 2003 CAFR. This report was delayed as a result of numerous political, legal and compliance challenges facing the City. These challenges were related to the under funding of the City's pension system and misappropriation of enterprise fund assets which took place over a period of approximately 20 years.

- Directly supervise eight Principal Accountants and indirectly supervise 65 employees
- Oversaw the implementation of a financial reporting system.

#### Principal Accountant

5/2005-5/2006

Working under the Auditor & Comptroller, I was responsible for the oversight and management of the Audit and Systems divisions of the City of San Diego. My responsibilities included, revenue auditing, internal auditing, performance auditing and the implementation of a data warehouse. In this capacity, I oversaw the production of the Auditor and Comptroller's First Annual Report on Internal Controls. This report was a comprehensive citywide risk assessment of financial reporting controls using the COSO framework. The report was a foundation for remediation efforts related to correcting the financial reporting irregularities previously experienced by the City.

- Directly supervised three Principal Accountants and indirectly supervised 14 employees.

### Santa Barbara County Auditor-Controller, Santa Barbara, CA

#### Accountant - Auditor 3

3/2004-5/2005

- Overseeing junior staff on audits and reviewing their work.
- Performing financial, operational and compliance audits.
  - Performing internal control reviews.
  - Preparing audit and review reports.
  - Planning and developing audit and review methodologies.

#### Accountant - Auditor 2

9/2003-3/2004

- Performing financial, operational and compliance audits.
  - Performing internal control reviews.
  - Preparing audit and review reports.

#### Accountant - Auditor 1

8/2002-9/2003

- Performing financial, operational and compliance audits.

### UCSB, Santa Barbara, CA

#### Information Systems Analyst

4/2001-4/2002

- Providing technical support to administrative staff.
- Researching and evaluating hardware and software applications.
- Providing technical support for desktops, server applications and hardware.
- Installing network and server components.
- Creating illustrations and schematics of the Facilities Fiber Optic Network.

References and additional experience are available upon request

### III. Timeline Modifications

implemented. By the time the ERP system is implemented, the City should be current on audits of its CAFRs and should have sufficient resources to focus on internal controls over financial reporting.

Additionally, the nature and structure of the City's internal controls are anticipated to change (and be enhanced) as a result of ERP implementation. City management believes that documenting and assessing internal controls for the new ERP system will add significantly more value than documenting and assessing internal controls for the current accounting system that is more than 30 years old and is planned to be replaced in the near-term.

#### Remedial Category – Internal Controls

79. The City has taken a number of steps to quantify the impact and correct its financial statements resulting from deficiencies in internal controls related to capital asset accounting. The City should continue to monitor the internal controls over these areas to ensure that potential errors in the future are detected and corrected in a timely manner. (Page M-20)
80. A number of deficiencies in the internal controls related to accounting for accounts receivable were identified. The City should develop and implement policies and procedures to reconcile, support, and review period end accounts receivable balances. (Page M-21 & M-22)

#### Updated Status:

The original completion date of June 2007 will not be met for full remediation of these items. Kroll items 79 (capital asset accounting) and 80 (accounts receivable reconciliations) both contain numerous subprocesses which are being prioritized based upon internal control importance.

The City's capital asset accounting process resulted in 20 restatements to the CAFR for the fiscal year ended June 30, 2003. As a result, this area requires more attention and therefore more documentation than other areas.

The City's accounts receivable balance is comprised of data from many different sub-systems. Each sub-system may require a unique reconciliation process which translates into documenting more subprocesses.

Due to unanticipated Auditor and Comptroller Office resource requirements related to supporting prior year Comprehensive Annual Financial Reports (CAFRs) audits and due to staffing shortages on the Kroll remediation team, some of the important Kroll remediation items related to financial reporting will not be completed by the due dates stated in my memorandum dated August 24, 2006. At the time my memorandum was issued, the City expected that audited CAFRs for fiscal years 2003-2005 would be issued by February 16, 2007.

The 2003 audited CAFR was not issued until mid March 2007 and the 2004-2005 CAFRs have not been issued to date. Auditor and Comptroller staff resources that were planned to assist with Kroll remediation efforts will not be available until the City is current with audited CAFRs.

Some of the more significant Kroll items impacted by timeline modifications are discussed below.

#### **Remedial Category – Independent Auditors**

36. A reputable independent auditing firm should be retained by the City's new Audit Committee which should in connection with the annual audit of the financial statements of the City for the fiscal year ending June 30, 2008, conduct an audit of the City's internal controls (emphasis added). (Pages 248, M-3 & M-4)

#### **Remedial Category – Financial Reporting**

58. The Mayor and Chief Financial Officer should annually include in the City's CAFR a signed management report on the financial statements and disclosures which include a statement of the City's responsibility for establishing and maintaining an effective system of internal control over financial reporting and disclosures; a statement setting forth the City's assessment of the effectiveness of the internal controls (emphasis added); a statement that based on their knowledge, the CAFR does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the CAFR not misleading; and a statement that the financial statements and other information included in the CAFR fairly present in all material respects the net assets and activities of the City for the period presented. (Pages 248, 249 & M-4)
59. The chief executive officer and principal accounting officer of each component unit of the City should include annually with its stand alone financial statements a signed management report substantially in the form described for the Mayor and CFO (emphasis added). (Pages 249 & M-4)

#### **Updated Status:**

Updated status relates to the areas of items 36, 58 and 59 that are underlined above. The audit of internal controls by an independent auditing firm is directly related to City management's assessment of the effectiveness of internal controls. City management believes audit of the City's internal controls by a reputable independent auditing firm should not take place until the City's new Enterprise Resource Planning (ERP) system has been



OFFICE OF MAYOR JERRY SANDERS  
CITY OF SAN DIEGO

MEMORANDUM

Date: February 21, 2007  
To: Honorable Members of the City Council  
From: Mayor Jerry Sanders *JSL*  
Subject: Kroll Remediation Status Report Number 4, prepared for  
March 5, 2007 Council Meeting

This is the Fourth in a series of status reports regarding Kroll Remediation efforts. To date, approximately 53 or 44% of the 121 Kroll remediation items have been completed, or are substantially complete and more than 25 additional items are in-process. Previous status reports were issued on October 5, 2006, October 30, 2006 and November 22, 2006. On March 5, 2007 my staff will meet with you to discuss the following:

- Status of remedial items completed as of February 16, 2007
- Status of remedial items in-process as of February 16, 2007
- Revisions to the Disclosure Practices Working Group

The status of all Kroll remediation items will be provided to Mr. Stanley Keller, Independent Monitor, for observations and comments. Any conclusions made by him will be provided to the City Council for its review.

Cc: City Attorney  
Chief Operating Officer  
Chief Financial Officer  
Stanley Keller, Independent Monitor  
Independent Budget Analyst  
SDCERS  
John Dyer

Attachment A - CFO Resume

Attachment B - City Attorney Report Regarding Remediation Measures Requiring Changes  
to the City Charter, and Related Matters

Attachment C - Establishment of a Charter Review Committee

Attachment D - Disclosure Practices Working Group Controls and Procedures

Attachment E - Status of Kroll Remediation Items Involving SDCERS

# I. Remedial Items Completed

## A. Items Previously Reported Complete

Kroll Item #	Kroll Category	Memo Reference	Additional Action Required		
			City Attorney	City Council	Mayor
7-12	Organizational Structure	10/5/2006			
24	Audit Committee – Formation and Duties (whistleblower procedures)	10/30/2006		Note A	
45	Budget Policies and Practices	10/30/2006			
46-47	City Actuarial Services	10/5/2006			
48(i)	Deferred Maintenance	10/5/2006			
49	Disclosure (DPWG)	11/22/2006		Note B	
54-57	Financial Reporting	10/30/2006			
57.1	Financial Reporting	10/5/2006			
66	Forecasting/Projections	11/22/2006			
74	Interest Allocation	10/30/2006			Note C
84-85	Reconciliation of Accounts	10/30/2006			Note C
107-108	City Funding of SDCERS	11/22/2006			
107.1	City Funding of SDCERS	10/5/2006			

### Notes:

- A. Audit Committee to assume selected areas of responsibility for "whistleblower" policies and procedures
- B. City Council action required to direct the City Attorney to modify the Municipal Code to change the membership of the Disclosure Practices Working Group (DPWG)
- C. Internal control operating design is complete; operating effectiveness (testing) to be performed



## I. Remedial Items Completed

### B. Items Completed During this Reporting Period

Kroll Item #	Kroll Category	Memo Reference	Additional Action Required		
			City Attorney	City Council	Mayor
1-6	Oversight Monitor	2/16/2007			
15	Staff Qualifications	2/16/2007			
18	Audit Committee – Formation and Duties (Long-Term Plan)	2/16/2007			Note D
19	Audit Committee – Formation and Duties (Eliminate FROB)	2/16/2007	Note E		
21	Audit Committee – Formation and Duties (Scheduled Meetings)	2/16/2007			
42	Ethics	2/16/2007		Note F	
43	Budget Policies and Practices	2/16/2007		Note G	
51	Disclosure (City Attorney Confirmation)	2/16/2007			Note H
52	Disclosure (City Council Review Period)	2/16/2007			
53	Disclosure (DPWG and Audit Committee)	2/16/2007		Note I	
71	Information Technology – Financial Reporting Systems	2/16/2007			Note J
73	Information Technology – E-Mail Systems	2/16/2007			Note K
82	Procurement	2/16/2007			Note H
89	Risk Management	2/16/2007			
96	Training	2/16/2007		Note L	
97	SDCERS Financial Reporting	2/16/2007			
98	SDCERS Internal Controls	2/16/2007			
99	SDCERS Actuarial Services	2/16/2007			
100-101	SDCERS Investment Advisors	2/16/2007			
103	City Funding of SDCERS	2/16/2007			
106	City Funding of SDCERS	2/16/2007		Note M	
113	SDCERS Organizational Structure	2/16/2007			
114	SDCERS Staff Qualifications	2/16/2007			
119,121	SDCERS Board Structure	2/16/2007			

## I. Remedial Items Completed

### Notes:

- D. Establishment of a Charter Review Committee; part of the committee's responsibilities include the long-term Audit Committee plan
- E. City Attorney to eliminate Financial Reporting Oversight Board (FROB) as redundant to the new Audit Committee
- F. Improper influence Ordinance is with Rules Committee for action
- G. City Council to review budget in April 2007
- H. Internal control operating design is complete; operating effectiveness (testing) to be performed
- I. Continued by City Council
- J. Short-term plan complete; long-term plan to be completed as part of ERP project
- K. Short-term plan complete; long-term plan scheduled for completion by September 2007
- L. Financial training budget to be submitted to City Council as part of midyear budget adjustment
- M. The repeal of "Waterfall" is in the process of being docketed with City Council

### **Remedial Category – Oversight Monitor**

1. Appoint a Monitor to oversee the implementation of and compliance with the Remediation Plan. (Pages 263 & M-14)
2. The Monitor should be selected by the Mayor in consultation with the City Council and subject to the approval of the SEC and should be an independent person of suitable standing, independence and experience for the assignment. (Pages 263 & M-14)
3. The Monitor should have complete and unfettered access to all City and SDCERS personnel and records. (Pages 263 & M-14)
4. The Monitor should make quarterly reports to the City and the SEC on the City's progress. (Pages 263 & M-14)
- 4.1 City Monitor quarterly reports should be made public in an appropriate manner including on the City's website. (Page M-14)
5. The Monitor should serve a term of no less than three years and should be provided adequate resources to carry out the duties of his office. (Pages 263 & M-14)
6. The SEC should have the right, upon request, to expand the scope of the Monitor's duties following consultation with the City. (Pages 263 & M-14)

**Status:** Complete. On January 16, 2007, the City Council approved a recommendation to hire Mr. Stanley Keller to provide the City with independent monitoring services called out in the Security and Exchange Commission's (SEC) order as well as in the Kroll report. In performing his work, the Monitor will have complete access to all City and SDCERS personnel and records. The Monitor was hired for a three year term and his

## I. Remedial Items Completed

agreement with the City calls for annual reports to the City and the SEC. The First report is due 120 days following the approval of the agreement by the City Council.

The announcement of the City's hiring of Mr. Keller for independent Monitoring services is on the City's website at the following address:

[http://www.sandiego.gov/mavor/pdf/keller\\_statement\\_1\\_16.pdf](http://www.sandiego.gov/mavor/pdf/keller_statement_1_16.pdf)

### Remedial Category – Staff Qualifications

15. The CFO should have significant experience with governmental operations, including accounting, financial reporting and applicable disclosure standards, rules and regulations. The CFO should in particular have experience in the preparation of a CAFR in accordance with governmental accounting standards and offering statements for a municipal issuer. (Pages M-1 to M-2)

**Status:** Complete. The City hired its first-ever CFO, Mr. Jay Goldstone, who started on January 23, 2006. Mr. Goldstone has significant experience with government operations, including accounting, financial reporting and applicable disclosure standards, rules and regulations. See Attachment A for Mr. Goldstone's resume.

### Remedial Category – Audit Committee Formation and Duties

18. The City should establish a three member Audit Committee comprised of two members from the public and one City Council Member. The public members would be nominated by the Mayor and confirmed by the City Council. (Pages 251 & M-6)

**Status:** Short-term action complete. My memorandum to the City Council dated October 31, 2006 had a long-term and short-term plan for the Audit Committee. A long-term plan is required because a City Charter change is necessary to fully meet the Audit Committee recommendations identified in item 18 above. Refer to Attachment B for the City Attorney's letter dated September 1, 2006, regarding Kroll Audit Committee conflicts with the City Charter. The City recently established a Charter Review Committee (refer to Attachment C). One of the areas the committee will focus on is "What Charter modifications are necessary to implement the Kroll recommendations and other financial reforms?"

On December 6, 2006 the City Council directed the City Attorney to prepare an ordinance to amend the Municipal Code to form an interim audit committee. The City Council approved the establishment of a temporary Audit Committee on January 9, 2007 (Council item 332b). Additionally, the Council confirmed the appointments of three Council members to the temporary audit committee (item 333).

## I. Remedial Items Completed

City Council meeting results for the above referenced items can be found on the City's website at the following address:

<http://clerkdoc.sannet.gov/Website/council-meeting-results>

19. The City's Financial Reporting Oversight Board should be eliminated as redundant to the Audit Committee. (Page M-6)

**Status:** City Council action complete. At its December 6, 2006 City Council meeting, the Council directed the City Attorney to eliminate the Financial Reporting Oversight Board (FROB) as redundant to the temporary Audit Committee.

The City Attorney's Office is planning to complete this action with other code changes which would reassign the FROB responsibilities, and define the Audit Committee responsibilities further. Anticipated completion date is April 2007.

21. The Audit Committee should meet quarterly, or more often if necessary, with the City's independent auditors, the City's Auditor General and the CFO. (Page 252)

**Status:** The Council amended the Meetings of the City Council and Standing Committees for the period January 1, 2007 through December 31, 2007 to add the Audit Committee (Council item 332c). Ten meetings are scheduled for calendar year 2007.

City Council meeting results for the above referenced item can be found on the City's website at the following address:

<http://clerkdoc.sannet.gov/Website/council-meeting-results>

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### Remedial Category – Ethics

42. To discourage any improper influence of the professionals who serve as "gatekeepers" to the public financial reporting process of the City, the Municipal Code should be amended to add criminal penalties for such conduct. It should be unlawful for any elected official, or employee of the City, or anyone acting under their direction, to take any action to corruptly influence, coerce, manipulate or mislead any independent certified public accountant engaged in the performance of an audit of the financial statements of the City or its component units, or outside legal counsel performing services for the City in connection with an offering statement of the City, or any actuary performing an actuarial valuation in connection with the preparation of the City's or SDCERS's CAFRs, or employees of a bond rating agency performing a credit rating of the City's bonds. (Page M-6)

**Status:** City Attorney action complete. The City Attorney prepared an ordinance and submitted it for City Council Action on November 1, 2006. On November 13, 2006, at the Special City Council Financial Hearing, the ordinance was referred to the Rules Committee. The Rules Committee is currently coordinating with the City Attorney's Office to docket the item. The ordinance should be reviewed at a February or March Rules Committee meeting.

## I. Remedial Items Completed

### Remedial Category – Budget Policies and Practices

43. In order to maintain current service levels and address issues such as deferred maintenance, the City must reduce expenditures by improving efficiency, increasing the current revenue base, and seeking alternative revenue sources. (Page M-14)

Mave to  
Ag 1/2

*In-process*  
**Status:** ~~Mayoral action complete.~~ Supporting data described below will be included in the 2008 budget to be submitted to the City Council on April 13, 2007.

I presented the City's first five-year financial plan to the City Council on November 29, 2006. The plan addresses deferred maintenance, reducing expenditures via various methods, such as, elimination of positions; business process engineering and streamlining; employee benefit adjustments; debt refinancing; budget clean-up; release of encumbered funds; transfer of inactive fund balances; establishing a property business improvement district; leveraging city assets and managed competition. Revenues are projected to increase through normal growth.

I realize that the Financial Outlook is only a tool to help produce a comprehensive, long-range analysis of the City's general fund revenues and expenditures. The five-year financial outlook will be regularly updated and will be used to assist with the preparation of the City's annual budget. The plan can be accessed on the City's website at:

[http://www.sandiego.gov/mavor/pdf/five\\_year\\_plan\\_11\\_15.pdf](http://www.sandiego.gov/mavor/pdf/five_year_plan_11_15.pdf)

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### Remedial Category – Disclosure

51. The City Attorney or City Attorney staff member should collect information relevant to public filings and bond offerings and should confirm, in writing, the accuracy of this information in the City's public documents. (Page M-25)

**Status:** Complete (internal control operating effectiveness to be tested upon the City's issuance of public filings or bond offerings). The Disclosure Practices Working Group (DPWG) adopted Controls and Procedures in October 2005 (refer to Attachment D) that require the City Attorney's Office to collect information relevant to public filings and bond offerings and to confirm, in writing, the accuracy of this information.

52. The City Council should have at least two weeks to review substantially completed drafts of a preliminary offering statement before it is asked to vote to approve the final document. (Pages 263 & M-14)

**Status:** Complete. The DPWG adopted Controls and Procedures in October 2005 that require it to provide the City Council over two weeks of review time before the City Council is asked to approve final offering documents. Refer to Article VI of the DPWG Controls and Procedures which are included as Attachment D.

## I. Remedial Items Completed

In the most recent offering statements (Ballpark Refunding and Water System Financing), the City Council was provided with over three weeks of review time. Documentation of over three weeks of lead time is included in the following Independent Budget Analyst (IBA) Reports.

- IBA Report Number: 07-7, Refunding of the Ballpark Bonds
- IBA Report Number: 07-8, Subordinated Water Revenue Notes, Series 2007A

53. The DPWG should report to the City's new Audit Committee. (Pages 249 & M-5)

**Status:** Mayoral task complete. The Mayor's Office previously submitted a Request for Council Action that the City Council direct the City Attorney to amend the Municipal Code for certain changes to the DPWG (refer to Council item 330 and my memorandum dated November 22, 2006). At the December 6, 2006 Council meeting, the item was continued until the independent monitor/consultant is hired and could provide input.

I recommend that the Council add the requirement to item 330 that the DPWG meet periodically (on an as needed basis) with the City's new Audit Committee to discuss the City's disclosure controls and procedures.

### Remedial Category – Information Technology, Financial Reporting Systems

71. The City should implement and utilize an automated financial reporting system to prepare the financial statements and complete the year-end closing. The City should maintain documentation supporting adjustments to facilitate the review of financial data. (Page M-15)

**Status:** Short-term plan complete. To facilitate automated financial reporting and financial documentation, the City completed the production phase of the data warehousing and business intelligence project on January 5, 2007. The application can be accessed via the following link:

<http://intra.sannet.gov/businessobjects/login.do>

The long-term plan to remediate Kroll item 71 is the implementation of an Enterprise Resource Planning (ERP) system. Refer to item 67 in section II.

### Remedial Category – information Technology, E-Mail Systems

73. All City "Post Offices" should be centrally operated, maintained, and backed up. Consolidating systems and personnel will improve economy and ease maintenance. It will also ensure consistent data retention systems, policies, and procedures are used for City information. (Page M-26)

## I. Remedial Items Completed

**Status:** Short-term plan complete. The short-term plan was to update the e-mail records retention policies. The long-term plan is the migration of the City's e-mail systems to Microsoft Outlook/Exchange and into one centrally managed system. The original due date for Microsoft Outlook/Exchange and one centrally managed system was June 2007. This has been revised to September 2007.

For background information, in early 2006, the Mayor created an e-mail task force to evaluate e-mail retention policies and system practices across City government. As a result of these efforts, the task force concluded that there were two distinct pieces of e-mail retention: records management and disaster recovery. After careful review, it was determined that the existing records management policies were acceptable, but that disaster recovery policies (that required keeping backups of all e-mails for just two weeks) required modification.

To that end, the task force recommended and the Chief Information Officer implemented (in October 2006) a revised procedure of retaining backups of the e-mail system for six months with a provision for extraordinary circumstances. During extraordinary circumstances (as determined by the Mayor and his advisors, "special circumstances" include external investigations, law suits, etc.), the six month window for maintaining backups can be extended until the special circumstances have elapsed.

### Remedial Category – Procurement

82. The City should review procurement procedures to ensure compliance with all applicable policies, the proper segregation of duties, and the proper safeguard of requisition forms. (Page M-24)

**Status:** Complete (internal control operating effectiveness to be tested by March 31, 2007). On October 9, 2006, the Purchasing and Contracting (P&C) department was created to centralize, consolidate and streamline procurement resources and processes associated with contract pre-award operations for commodities, services, consultant and construction into one department (refer to City Council item 150). Policies and procedures have been drafted and are pending formal adoption for non-engineering consulting services which require contract execution by P&C. Additionally, a Designation of Authority memorandum was issued on November 2, 2006 to delineate persons who have the authority to initiate and negotiate a contract, lease, or other document or amendment, as well as persons who have the authority to sign and award contracts.

A formal documented process for P&C has been completed for compliance with Municipal Code item 22.3223. This requires that the City Council approve awards of contracts exceeding \$250,000 to a single consultant during any fiscal year. Documentation includes an internal control matrix, process flow, process narrative and identification of significant control activities.

## I. Remedial Items Completed

Additionally, user profiles within OPIS (Online Procurement Information System) have been remediated to ensure the proper segregation of duties. Finally, Central Stores Department Instruction Number DA-1.01 was issued to ensure the proper and accurate issuance and handling of City financial requisition forms.

### Remedial Category – Risk Management

89. The City should improve monitoring of Workers' Compensation cases and ensure that payments are made in a timely manner to avoid penalties. (Page M-24)

**Status:** Complete. The City's Risk Management Department has improved the monitoring and processing of workers' compensation permanent disability penalty payments. This remediation item is the result of a finding by Macias Ginni & O'Connell during its fiscal year 2004 financial statement audit. The finding relates to a 10% penalty that is required on any permanent disability payment that is more than 14 days after the last temporary disability payment. The City's improvement in reducing penalty incidents and amounts is shown below:

Fiscal Year	Penalty Incidents	Penalty Amounts
2003	302	\$90,991
2004	253	\$57,350
2005	144	\$34,827
2006	134	\$37,337
2007*	45 or 90 annualized *	\$10,786 or \$21,572 annualized *

\* The penalty incidents and amounts for fiscal year 2007 are for the first six months of the year (July-December 2006). The penalty incidents and amounts have been annualized, by multiplying by two, for comparison purposes to prior fiscal years.

### Remedial Category – Training

96. Funding should be added to the budget to ensure adequate training of personnel to ensure that they remain current on financial reporting standards. (Pages 246 to 247)

**Status:** Continual. Many of the accounting staff within the Auditor & Comptroller's Office has gone to at least one training session during this fiscal year. Specific funding will be included in the fiscal year 2008 budget for additional training opportunities in both this Auditor's budget as well as in the Financial Management.



## I. Remedial Items Completed

### Remedial Category – SDCERS Financial Reporting

97. The Audit Committee concurs with actions being taken by the Retirement Administrator to establish a financial reporting function within SDCERS. (Page M-9)

**Status:** Complete. Refer to SDCERS letter dated January 31, 2007 regarding the Status of Kroll Remediation (see Attachment E).

### Remedial Category – SDCERS Internal Controls

98. SDCERS should develop a comprehensive methodology to identify, track, and recover overpayments made to deceased pensioners. (Page M-25)

**Status:** Complete. Refer to SDCERS letter dated January 31, 2007 regarding the Status of Kroll Remediation (see Attachment E). I will forward my recommendation to the SDCERS' Board that this item be tested for internal control operating effectiveness no later than fiscal year 2008. Additionally, I recommend that the internal control testing results and documentation be presented to the SDCERS Audit Committee.

### Remedial Category – SDCERS Actuarial Services

99. SDCERS should rebid the contract for the performance of its actuarial valuation every five years and that the actuary not be engaged for more than two five-year terms. (Pages 260 & M-12)

**Status:** Complete. Refer to SDCERS letter dated January 31, 2007 regarding the Status of Kroll Remediation (see Attachment E).

### Remedial Category – SDCERS Investment Advisors

100. SDCERS should require its investment consultants and fund managers to annually complete a Vendor Disclosure Form that calls for disclosure of all information regarding remuneration paid or received related to funds managed for SDCERS, as well as its business dealings with the SDCERS investment consultant. (Pages 258 & M-10)
101. Investment consultants and managers should be advised that a failure or delay in filing the annual disclosure will result in a penalty, including termination of services. (Pages 258 & M-10)

**Status:** Complete. Refer to SDCERS letter dated January 31, 2007 regarding the Status of Kroll Remediation (see Attachment E). I will forward my recommendation to the SDCERS' Board that these items be tested for internal control operating effectiveness no later than fiscal year 2008. Additionally, I recommend that the internal control testing results and documentation be presented to the SDCERS Audit Committee.

## I. Remedial Items Completed

### Remedial Category – City Funding of SDCERS

103. The City should contribute to SDCERS annually the Annual Required Contribution, as calculated by SDCERS actuary, including an amount sufficient to amortize existing UAAL over a reasonable period of time that assures that current taxpayers are paying for the full cost of services rendered by employees of the City and not passed on to future generations. (Pages 259 & M-11)

**Status:** Complete. The Mayor's Five Year Plan contains full ARC (Annual Required Contribution) contributions over an amortization period in compliance with the "Gleason Settlement." The City's budget for fiscal year 2007 contains a contribution of \$162 million to pay the full ARC. This contribution was made at the beginning of the fiscal year (July 2006).

Additionally, the plan for fiscal years 2008-2012 provides for payment of ARC plus to eliminate negative amortization of the UAAL (Unfunded Actuarial Accrued Liability). The ARC plus contribution amounts to an additional \$27.1 million annual contribution over this period, or \$135.5 million in total.

The survey results can be accessed on the City's website at:

[http://www.sandiego.gov/mayor/pdf/five\\_year\\_plan\\_11\\_15.pdf](http://www.sandiego.gov/mayor/pdf/five_year_plan_11_15.pdf)

106. The City should not use its contribution to pay for any benefits other than retirement benefits and the related costs of administering the Plan. Thus, no portion of the City's annual contribution to SDCERS should be credited against the City's obligation to pay retiree healthcare costs, or for any other of the so-called "Waterfall" payments, unless and until the City pays the required ARC. (Pages 259 & M-11)

**Status:** City Attorney action complete. The Municipal Code change to repeal the "Waterfall" payments is in the process of being docketed.

### Remedial Category – SDCERS Organizational Structure

113. The controlling legal documents must make the Board's authority clear related to investment policy, actuarial assumptions, system budget and policies, retention of outside professionals, and administrative rules. (Page M-25)

**Status:** Complete. Refer to SDCERS letter dated January 31, 2007 regarding the Status of Kroil Remediation (see Attachment E).

## I. Remedial Items Completed

### Remedial Category – SDCERS Staff Qualifications

114. The chief accounting officer of SDCERS should have adequate prior experience with investment operations and financial reporting and disclosures. (Pages 258 & M-10)

**Status:** Complete. Refer to SDCERS letter dated January 31, 2007 regarding the Status of Kroll Remediation (see Attachment E).

### Remedial Category – SDCERS Board Structure

119. SDCERS should have standing committees to address board governance, compensation and evaluation of the Retirement Administrator, investments, and an audit and compliance committee. (Pages 256 & M-9)
121. SDCERS must be free to retain its own independent legal counsel. (Pages 260 & M-12)

**Status:** Complete. Refer to SDCERS letter dated January 31, 2007 regarding the Status of Kroll Remediation (see Attachment E).

## II. Remedial Items In-Process

### A. Items In-Process Previously Reported

Kroll Item #	Kroll Category	Memorandum Reference	Updated status?
13-14	Organizational Structure	October 5, 2006	No
20, 22-23	Audit Committee, Formation and Duties	October 30, 2006	Yes *
44	Budget Policies and Practices	October 30, 2006	Yes *
52.1, 52.2	Disclosure	October 5, 2006	No
58-59, 64-65	Financial Reporting	November 22, 2006	No
75-80	Internal Controls	November 22, 2006	No
81	Personnel	November 22, 2006	No
83	Redevelopment Authority	November 22, 2006	No
86	Reconciliation of Accounts	October 5, 2006	No
87	Retirement Benefits	October 30, 2006, November 22, 2006	Yes *
88	Risk Management	November 22, 2006	No
90, 95	Training	November 22, 2006	No

\* see below

#### **Remedial Category – Audit Committee Formation and Duties**

20. The Audit Committee should establish a written charter. (Pages 251 & M-6)
22. The Mayor, CFO, City Attorney, *Independent Budget Analyst (added)* and City Council should have the authority to make requests of the Audit Committee and Auditor General to perform internal audits of material matters they reasonably believe to be warranted. (Page 252)
23. With the assistance of the CFO and Auditor General, the City's independent auditors would be retained by, report to and take direction from the Audit Committee. (Page 252)

**Updated Status:** In process. The temporary Audit Committee was created by the City Council during its January 9, 2007 Council meeting (refer to section I of this memorandum). The Audit Committee is in the process of establishing a written Charter that will address its duties and responsibilities. The Audit Committee is required to develop and recommend a Charter containing the duties and responsibilities of the Committee for further discussion and approval by the City Council by April 9, 2007 (90 days from January 9, 2007).

#### **Remedial Category – Budget Policies and Practices**

44. Ongoing expenditures should be supported by ongoing revenues; capital projects should identify all future cost considerations and financial impacts, including direct

## II. Remedial Items In-Process

and indirect costs for each Enterprise Fund; activities supported by user fees should be fully cost recoverable; discretionary General Fund revenues should not be earmarked; increase the General Fund reserve to the range of 7-10%; budget development should be guided by a long term or strategic plan proposed by the Mayor and adopted by the City Council; and after adoption, annual budgets should be amended only for urgent needs. Specific funding sources should be identified to pay for these needs. (Pages M-14 & M-15)

**Updated Status:** A draft General Fund reserve policy was presented to the Budget and Finance Committee during its November 29th Committee meeting. The draft policy identifies a reserve account, separate from the "deep reserves," which will serve as a contingency for unanticipated expenses approved by City Council during a given fiscal year. It is anticipated that the General Fund policy will be finalized and presented to the full City Council by June 2007.

### Remedial Category – Retirement Benefits

87. The City Council and employees should develop realistic retirement plan parameters for future City hires. This includes positioning the City to attract and retain the talent needed to meet the citizens' expectations for services, not be viewed as providing excessive benefit levels, and creating a plan the City can afford. (Page M-25)

**Status:** Partially Complete. To address this item, the City is performing the following three evaluations:

- Actuarial evaluations of the cost implications of formula changes to the existing retirement systems (in-process)
- Benchmark study of Police Compensation and benefits for all employees (complete, see below)
- Benchmark study of Fire Compensation and benefits for all employees (in-process)

On December 21, 2006, the City issued an independent and comprehensive study of "The City of San Diego Police Classification Compensation and Benefits Survey Results." The Fact Sheet can be accessed on the City's website at:

[http://www.sandiego.gov/mavor/pdf/fs\\_pdpav.pdf](http://www.sandiego.gov/mavor/pdf/fs_pdpav.pdf)

The survey results can be accessed on the City's website at:

<http://www.sandiego.gov/mavor/pdf/pdsurvey.pdf>

On February 14, 2007, the City issued an independent and comprehensive study of "The City of San Diego Fire Classification Compensation and Benefits Survey Results." The Fact Sheet can be accessed on the City's website at:

[http://www.sandiego.gov/mavor/pdf/fire\\_survey\\_2\\_15.pdf](http://www.sandiego.gov/mavor/pdf/fire_survey_2_15.pdf)

## II. Remedial Items In-Process

### B. Items In-Process During this Reporting Period

#### Remedial Category – Information Technology, Financial Reporting Systems

67. By June 30, 2007, evaluate the information technology needs of the City, including benchmarking of existing systems against available systems suitable for management of the City's finances and the preparation of timely and accurate CAFRs and budgets. (Pages 247 & M-3)

**Status:** In-process. As background information, for the majority of its financial and accounting functions, the City currently relies on mainframe-based systems, many of which were developed more than 30 years ago.

The City recently completed a detailed Enterprise Resource Requirements plan prior to issuing a Request for Proposals (RFP) on January 19, 2007 to replace its aging financial and information management systems. As early as the City's 2001 Information Technology Strategic Plan, the City recognized a requirement to evaluate options for replacing core financial and human resources systems.

The City plans to select an Enterprise Resource Planning (ERP) vendor by March 2007. The news release for the RFP can be accessed on the City's website at:

[http://www.sandiego.gov/mavor/pdf/erp\\_factsheet\\_1\\_19.pdf](http://www.sandiego.gov/mavor/pdf/erp_factsheet_1_19.pdf)

Additionally, on February 5, 2007, the City Council adopted item 201 "Approving in Concept a Project to be Known as the Enterprise Resource Planning Core System."

#### Remedial Category – SDCERS Financial Reporting

102. The Retirement Administrator and CFO of SDCERS should annually include in the SDCERS' CAFR a signed management report on the financial statements and disclosures which include a statement of SDCERS' responsibility for establishing and maintaining an effective system of internal control over financial reporting and disclosures; a statement setting forth SDCERS' assessment of the effectiveness of the internal controls; a statement that based on their knowledge, the CAFR does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the CAFR not misleading; and a statement that the financial statement and other information included in the CAFR fairly present in all material respects the net assets and activities of SDCERS for the period presented. (Pages 257 & M-9)

**Status:** In-process. Refer to SDCERS letter dated January 31, 2007 regarding the Status of Kroll Remediation (see Attachment E). SDCERS intends to include a management report on the financial statements and disclosures (that meet the requirements of Kroll item 102) with its 2006 Comprehensive Annual Financial Report (CAFR).

## II. Remedial Items In-Process

### Remedial Category – City Funding of SDCERS

104. For purpose of calculating annual funding requirements, the UAAL should reflect a prudent view of economic reality and include within it the costs of the Corbett settlement. (Pages 259 & M-11)

**Status:** In-process. SDCERS Board action approved and directed the actuary to include the costs of the Corbett settlement and 13<sup>th</sup> check. The Actuary report dated January 2007 contains these components in the UAAL. The Actuarial Valuation Report was presented at the SDCERS board meeting dated January 19, 2007. The link to the SDCERS board meeting agenda follows:

[http://www.sdcers.org/agendas/2007/january/bd\\_admin\\_1\\_19\\_07.pdf](http://www.sdcers.org/agendas/2007/january/bd_admin_1_19_07.pdf)  
(refer to page 6, item IV.A.1)

The January 2007 Actuarial Report can be accessed on SDCERS website at:

[http://www.sdcers.org/images/pdf/city\\_of\\_san\\_diego\\_actuarial\\_valuation\\_report\\_1\\_12\\_07\\_final.pdf](http://www.sdcers.org/images/pdf/city_of_san_diego_actuarial_valuation_report_1_12_07_final.pdf)  
(refer to pages 29 and 31)

In addition, at its February 2007 Board Meeting, the SDCERS Board heard recommendations from Cheiron regarding changes to the amortization schedule. The Board is expected to make a final decision at its March meeting. Other actuarial assumptions will be considered in 2008.

### Remedial Category – SDCERS Organizational Structure

112. To address Board authority and pursue administrative excellence, the controlling documents should be reviewed and, if necessary, modified to ensure that the Board has the necessary tools available to effectively and efficiently carry out its fiduciary duties. (Page M-25)

**Status:** In-process. Refer to SDCERS letter dated January 31, 2007 regarding the Status of Kroll Remediation (see Attachment E).

### Remedial Category – SDCERS Board Structure

120. SDCERS should adopt a formal charter for each committee which should be updated no less frequent than every three years. Pages 257 & M-9)

**Status:** In-process. The Audit Committee's charter has been adopted. Charters are being drafted for the other standing committees. Refer to SDCERS letter dated January 31, 2007 regarding the Status of Kroll Remediation (see Attachment E).

JAY M. GOLDSTONE

PROFESSIONAL EXPERIENCE

**CITY OF PASADENA, CALIFORNIA**

- Department of Finance  
Director of Finance

January 1996 to January 2006

Direct all aspects of the City's financial operations including its Electric and Water Utilities, Redevelopment Agency, Housing Authority, and Health Department. Prepare the City's \$508 million operating budget. Oversee the investment of nearly \$400 million in City funds. Responsible for purchasing, payroll, accounts payable, general accounting, information technology, and risk management. Prepare five year financial plans for the General Fund and Redevelopment Agency and ten-year financial plans the Electric Utility and Library Funds, assist in short and long-term planning. Handle the issuance and management of all debt; review and analyze potential business ventures for the City; participate in labor negotiations; and work closely with the City Council, providing it with continual financial information and guidance regarding the City's economic activities and outlook. During my tenure with the City of Pasadena, have issued over \$400 million in debt, including revenue bonds, pension obligation bonds, tax allocation bonds, certificates of participation, and Mello-Roos bonds.

**MARICOPA COUNTY, ARIZONA**

- Department of Finance  
Manager of Finance

November 1994 to August 1995

Planned, organized and directed the operations of the Department of Finance. Assigned work responsibilities to 59 professional and support staff; recommended and developed fiscal policy and procedures; established and monitored fiscal control procedures; prepared financial reports; analyzed the financial impact of proposed legislation; and work with all County department on various fiscal issues. Participated in the negotiations of a multi-year, multi-million dollar contract to privatize the County Hospital patient billing system.

**CITY OF RICHMOND, CALIFORNIA**

- Office of the City Manager  
Interim City Manager

February 1993 to January 1994

The City of Richmond has a nine member City Council, over 1,250 full time and part time employees and an annual operating and capital improvement budget of nearly \$220 million. Worked closely with the Mayor and City Council on all City related issues, implemented Council policies, served as intermediary between staff and the Council; worked with the 39 neighborhood councils, implemented Community Policing; completed the Environmental Impact Report (EIR) on the City's General Plan update; completed an EIR on a \$750 million Clean Fuels Project for a Chevron Refinery; negotiated financial and employment agreements with Chevron as part of its Project; negotiated development agreements, developed a balanced budget in light of State revenue transfers, developed and implemented various ordinances in order improve public beautification; and developed a public relations campaign in order to both improve the City's image and promote economic development.

- Department of Finance  
Director of Finance

May 1988 to November 1994  
(except as noted above)

Directed all aspects of the City's financial operations including its Port, Redevelopment Agency, and Housing Authority. Prepare the City's \$220 million operating and capital improvement budget. Oversaw the investment of City funds. Responsibility for purchasing, payroll, accounts payable, general accounting, and risk management. Under my direction, the City developed a five year financial plan to assist in short and long-term planning. Handled the issuance and management of all debt; reviewed, analyzed and participated in the negotiations of potential business ventures for the City; participate in labor negotiations; and work closely with the City Council, providing it with continual financial information and guidance regarding the City's economic activities and outlook.



## **CITY OF SANTA CLARA, CALIFORNIA**

### **- Finance Department**

Assistant Director of Finance

October 1985 to May 1988

Coordinated the preparation and presentation of the City's \$260 million budget. Supervised the daily investment of the City's \$200 million portfolio. Implemented the City's on-line Financial Management Information System, including validating System accuracy, establishing System balancing control procedures, revising operating and accounting procedures, and training City staff. Issued and managed debt. Prepared, monitored, and updated the City's five-year financial plan. Worked with City departments on financial related issues. Performed cost studies.

## **SAN MATEO COUNTY, CALIFORNIA**

### **- Department of Community Services, Director's Office**

Administrative Coordinator

1980 to 1985

### **- Department of Community Services, County Library**

Management Analyst III

1979 to 1980

### **- Department of Health and Welfare**

Management Analyst I/II/III

1976 to 1979

Prepared departments' budgets. Presented proposed budgets to Board of Supervisors. Prepared fiscal projections and monitored program revenues and expenditures. Negotiated and monitored contracts. Conducted studies and analyzed programs and services to determine cost effectiveness and usefulness. Established fiscal monitoring procedure to track both direct expenditures and the allocation of overhead to various funding sources.

## **EDUCATION**

Master of Business Administration

University of Santa Clara, CA

1983

- Course emphasis in Finance

Master of Public Administration

Arizona State University

1975

- Course emphasis in Municipal Administration

Bachelor of Science

University of Minnesota

1973

- Triple major in Political Science, Economics, and Business Admin.

## **PROFESSIONAL MEMBERSHIPS:**

Issuers' Advisory Group of the Municipal Securities Ruling Making Board (MSRB)  
Revenue & Taxation Committee - League of California Cities  
State Controller's Advisory Group on Financial Reporting  
Government Finance Officers Association  
California Society of Municipal Finance Officers (CSMFO)  
California Municipal Treasurers Association (CMTA)  
Former Member of the CDIAC - Technical Advisory Committee for Debt

Michael J. Aguirre

CITY ATTORNEY

Attachment B

September 1, 2006

REPORT TO THE HONORABLE  
MAYOR AND CITY COUNCIL

RE: REMEDIATION MEASURES REQUIRING CHANGES TO THE CITY CHARTER,  
AND RELATED MATTERS

### INTRODUCTION

The "Report of the Audit Committee of the City of San Diego" [Kroll Report] was presented to the San Diego City Council at its meeting on August 8, 2006. The report suggests serious deficiencies in the City's financial reporting obligations and proposes numerous remediation measures.

On August 24, 2006, the Mayor issued a plan to implement certain remedial measures. [Mayor's Report]. The Mayor's plan will be considered by the City Council at a special meeting on September 6, 2006.

The Kroll recommendations incorporated in the Mayor's plan include some items that would significantly change the City's auditing and financial reporting structure. The Mayor's report acknowledges that some Charter changes will be required to implement the recommendations.

Among other concerns, the recommendations to the Council suggest new committees and outside individuals be vested with decision making authority previously exercised by, and legally reserved to, elected officials. These types of changes conflict with the City Charter and, prior to implementation, will require a vote of the electorate on specific Charter amendments.

Failure to obtain the required Charter modifications prior to implementation would result in actions taken in excess of the jurisdiction of the offices of the Mayor and/or City Council (*Ultra vires* acts) rendering all such acts "void" from inception. Such actions could subject the City to liability for actions taken, or not taken, by persons asserting authority where none has been legally granted; subject persons acting under such deficient authority to exposure for which there would be none of the immunities associated with government service; and further complicate the ability of the City to resolve its issues with federal regulators and to re-enter the capital markets.

This initial report will highlight, by example, some of the suggested remediation measures that require changes to the City Charter and will provide recommendations for further action. In particular, this report focuses on:

1. Changes to the composition of the San Diego City Employees' Retirement System Board of Administration;
2. Changes to the Office of the City Auditor and Controller;
3. Creation of an "Audit Committee";
4. Appointment of a "Monitor"; and
5. Changes to the jurisdiction of the Office of the City Attorney to eliminate that office as attorney for the Retirement System.

## DISCUSSION

### I. The City Council may not Impact, by Ordinance, Charter-Established City Departments or Charter-Established Duties of City Officials.

A charter is the supreme law of a city, subject only to constitutional limitations and preemptive state law. *Domar Electric, Inc. v. City of Los Angeles*, 9 Cal. 4th 161, 170 (1994). "[I]t is well settled that a charter city may not act in conflict with its charter," and that "[a]ny act that is violative of or not in compliance with the charter is void." *Id.* at 171. This means that the City Charter's authority is greater than the authority of any ordinance enacted by the City's legislative body, the City Council. Should an ordinance or other action by a City Council conflict with what the charter provides, the City Council's action is void and unenforceable.

The City Council has the authority to place measures before the voters that propose changes to the City Charter, either at its own discretion, or as mandated after the presentation of certain certified voter petitions. See, *Howard Jarvis Taxpayers Assn. v. City of San Diego*, 120 Cal. App. 4th 374, 377-380 (2004). The actual changes to a City Charter may only occur by a vote of the electorate.

Established legal authority and City Charter section 26 preclude any Council action by ordinance that seeks to change a charter-established *department* of the City or a charter-established *duty* of a city official. Charter section 26 provides in pertinent part:

The Council shall by ordinance, by majority vote, adopt an administrative code providing for the detailed powers and duties of the administrative offices and departments of the City Government, based upon the provisions of this Charter. Thereafter,

*except as established by the provisions of this Charter*, the Council may change, abolish, combine, and rearrange the departments, divisions and boards of the City Government provided for in said administrative code, but such ordinance creating, combining, abolishing or decreasing the powers of any department, division or board shall require a vote of two-thirds of the members elected to the Council. The Council may by ordinance, if authorized so to do by the general law of the State, provide that any function of the City may be performed by the County or that any function of the County may be performed by the City, provided the respective legislative bodies authorize and approve such transfer and assumption of function. There may also be established a combined City and County district for the performance of any function. [Emphasis added].

Section 26 was assessed in *Hubbard v. City of San Diego*, 55 Cal. App. 3d 380 (1976). The court found that: "... the power of the council to 'change, abolish, combine, and rearrange the departments, divisions and boards of the City Government provided for in said administrative code' is limited by the words 'except as established by the provisions of this Charter.'" *Id.* at 387. The court then held, most unequivocally that:

We face the problem whether the council, under the charter, may create a department of city government not provided for by the charter and remove it from the supervision and control of the manager by designating that department a legislative department without regard to the powers and duties attempted to be given to it.

*We hold that the council cannot do so.*

*The council may not create a department of the city government, by whatever name it is given, which duplicates or infringes upon the specific powers or duties assigned by the charter to another department or, generally, to the manager."* *Id.* at 388. [Emphasis added].

Another San Diego case, *Dadmun v. City of San Diego*, 9 Cal. App. 549 (1908), prohibits the City Council from transferring the duties given to a city officer by the charter to another by ordinance. In *Dadmun*, the City Council passed an ordinance creating the office of special prosecutor to prosecute only municipal ordinance violations. The City Charter at that time provided that the prosecution of municipal ordinances was the duty of the City Attorney. The Court held that "the city council cannot relieve a charter officer of the city from the duties devolving upon him by the charter and designate another to perform those duties . . . . It follows, then, that the action of the city council in appointing a special prosecutor whose duty it should be to prosecute criminal violations of ordinances was unauthorized and void . . . ." *Id.* at 551.

These court decisions and City Charter section 26 limit the City Council's ability to take action by ordinance to implement the suggested "remediation measures" that conflict with existing Charter provisions establishing or assigning duties to City departments or officials. They similarly preclude the Mayor's office from implementing those changes administratively prior to Charter revision by the electorate.

## II. Changes to the Composition of the San Diego Retirement Board of Administration.

The Kroll report recommends several changes involving the San Diego City Employee Retirement System. One of the proposals is to change the size and composition of the Board that administers the System. Kroll Report, Appendix M-8. City Charter section 144 governs the composition of that Board. This proposed change conflicts with the existing charter. A change to the City Charter is required in order to change the composition of that Board.

## III. Changes Impacting the Office of Auditor and Comptroller.

The Kroll report recommends several changes that will impact the Office of the Auditor and Comptroller as it now exists. The duties of the Auditor and Comptroller are broad and varied under the City Charter and the San Diego Municipal Code. A partial summary of those duties is included in a memorandum prepared by this Office entitled "The Relationship between the City Offices of the Mayor and the Auditor and Comptroller under the Mayor-Council Form of Government" (January 23, 2006), a copy of which is attached. The proposed remedial measures eliminate the position of the Auditor and Comptroller and create five (5) new offices: an Auditor General, a separate City Comptroller, a Director of Financial Reporting, a Director of Financial Management, and a Director of Debt Management. It may also be appropriate to amend the Charter to clarify the role of the Chief Financial Officer.

The suggested restructurings in these offices will require amendments to the City Charter.

## IV. Creation of an Audit Committee.

The Kroll Report recommends the creation of a three-member Audit Committee, consisting of two citizen members and one member of the City Council. The two citizen members are to be appointed by the Mayor with Council confirmation, and will receive compensation. Appendix M-6. The Kroll report recommends that the City's independent auditors "should be retained by, report to, and take direction from, the Audit Committee." *Ibid.* The Committee is to be given the power to select and retain independent auditors, who will report only to it. *Ibid.* The City's Financial Oversight Board is to be eliminated as redundant to the Audit Committee. *Ibid.*

The Kroll Report recommends that the proposed new Auditor General report to the Audit Committee. The Audit Committee would set this official's annual compensation and the annual budget of this official's new department. The Auditor General can be removed from office for cause by the Audit Committee or upon the vote of three-quarters of the City Council. Appendix M- 5.<sup>1</sup>

The suggestion that the Audit Committee have the authority to set salaries and/or budgets conflicts with City Charter section 11.1, and related sections. Section 11.1 expressly forbids the City Council from delegating its responsibility to adopt ordinances to raise or spend public money, including "the annual budget ordinance, or any part thereof, and the annual ordinance setting compensation for City employees." *Also see* § 290 [City Council must set and adopt the terms of the salary ordinance and the City Budget]. The City Charter requires the City Council to approve the range of compensation for all City officials and the budget for all City departments. As noted in Part I above, the City Council may *not* by ordinance create an Audit Committee and provide it with powers that conflict with the Council's charter-required duties. This may only be accomplished by a change to the Charter.

If the Audit Committee is intended as an advisory committee, its proposed duties also conflict with another Charter section. The Kroll Report recommends the citizen members of this committee receive compensation. This recommendation conflicts with section 43(a) which forbids such compensation: "The members of such boards shall serve without compensation . . ." City Charter § 43(a). However, this may not become an issue as the Mayor's Report indicates that: "It is anticipated that members of the Audit Committee will not be compensated for serving on the Committee. *See*, Mayor's Report, p. 5.

The Kroll Report also recommends the Audit Committee retain and direct the City's independent auditors; and the Committee is to have ultimate authority over the office of Auditor General, including the absolute right to set the salary for the City Official and the budget for the department, and to remove this City Official for cause. This authority also conflicts with section 43(a) which provides: "The members of such boards shall . . . not . . . direct the conduct of any Department or Division."

The creation of the Audit Committee requires changes to the City Charter. The Mayor's suggested timeline for the creation of this committee must necessarily be deferred to coincide with the remainder of the ballot proposals for the November, 2008 election.

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<sup>1</sup> This position was reiterated by the authors of the Kroll report in an article August 30, 2006 in the San Diego Union Tribune "An Opportunity to Move Forward." They stated: "The audit committee also sets the compensation and budget for the auditor, which should allow them to do their oversight without undue influence from any branch of government."

V. Appointment of an Independent Monitor to Oversee the City's Remediation Plan.

The Kroll Report suggests the appointment of an independent "Monitor", a person who must have "complete and unfettered access to all City and SDCERS personnel and records." Appendix M-14. The SEC is to be given the right, whenever it chooses, to expand the duties of this Monitor. *Ibid*.

The Mayor's Report accepts this recommendation and indicates that the selection process has begun. The Mayor anticipates paying more than a million dollars a year for three years of this individual's services. Mayor's Report, p. 1. The Independent Budget Analyst recommends more public discussion on the necessity of this position, scope of work and funding requirements before the Council approves any contract for this individual. For several reasons, we agree that additional public discussion is essential to this process.

Under existing City Charter provisions, neither the Mayor nor the City Council may contract for the services of an individual that would include such a broad delegation of authority.

The Mayor has the authority under City Charter section 28 to hire certain experts and consultants. Those individuals contract with the City and receive their duties and direction from the City. The Monitor described in the Kroll report is plainly *not* such an individual.

Although the City would pay for this individual's services, the report contemplates that an outside agency would set the duties of this official, not the City. No aspect of the City Charter provides the Mayor or the City Council with the authority to select a private individual and provide them with "unfettered" access and authority over City affairs.<sup>2</sup>

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<sup>2</sup> City Charter section 40 gives broad authority to examine the affairs of the City to only one City Official, the City Attorney. It provides: "The City Attorney shall have charge and custody of all legal papers, books, and dockets belonging to the City pertaining to his office, and . . . may demand and receive from any officer of the City any book, paper, documents, or evidence . . . required for the purpose of the office." The *Dadmum* and *Hubbard* cases provide that the City Council may not contract for the services of an individual and grant powers that conflict with the powers already given by the City Charter to a City Official. Accordingly, the appointment of an independent Monitor would require a Charter amendment.

Monitors may be appointed to oversee the implementation of court-ordered remediation plans and given jurisdiction over certain affairs of a City in a appropriately filed legal proceedings. Likewise, they may be included in certain administrative proceedings, "consent decrees" and the like. The City is in discussions with the Securities and Exchange Commission regarding securities related issues. It is not inconceivable that a "Monitor" will be a required element of the resolution of our efforts with that agency. In such case, the term of service, and the role, of the person serving as the City's Monitor will be tailored to the specifications of services deemed to be required by the SEC and that person will have authority under well established legal authority. Adopting the "Monitor" suggested in the Kroll Report is inconsistent with the grant of jurisdiction required by the City Charter. It also adds nothing to the resolution of the monitoring functions which may be required by the SEC, and may in fact conflict with that process.<sup>3</sup>

#### VI. Changes to the City Attorney as Attorney for the Retirement System.

The Kroll Report recommends that the City's retirement system be free to retain its own independent counsel. Appendix M-12. San Diego Charter section 40 lists the duties it requires of the City Attorney. One of them is that "*The City Attorney shall be the chief legal adviser of, and attorney for the City and all Departments and offices thereof* in matters relating to their official powers and duties, except in the case of the Ethics Commission, which shall have its own legal counsel independent of the City Attorney." [Emphasis added]. San Diego Municipal Code section §22.1801(b) designates "the departments of the City of San Diego within the meaning of the Charter and ordinances of said City." One of the City Departments is "City Retirement." The City Retirement System is a City Department. It follows that the City Attorney is the System's Attorney by City Charter mandate.

The City Attorney's duty to provide legal services to the City has historically included providing services to the retirement system. However, this issue is currently the subject of litigation, and will ultimately be resolved in that forum. In the meantime, the suggested recommendation to permit this City Department to retain independent counsel conflicts with the

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<sup>3</sup> Federal courts can utilize outside monitors to observe, examine and scrutinize public corporations, police departments, unions and even industries entering into comprehensive settlement agreements to avoid further prosecution for wrongdoing. These monitors are given specific direction and duties by the Court. To insure the monitor is fully independent of the entity which it is scrutinizing, the monitor is chosen, employed and subject to replacement only by the Court. The Court appointed monitor is required to provide the utmost of honesty and candor to the Court. Failure to do so could place the monitor itself in contempt.

In the typical settlement or remediation agreement, the monitor is required to periodically report its findings to the Court.

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plain language of Charter section 40. To transfer that duty to another person would require a change to the City Charter.

### CONCLUSION

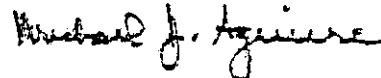
The recommendations in the Kroll Report involve complicated and interrelated changes to the City Charter and to many related portions of the San Diego Municipal Code. The changes will be more complex than the recent change to our trial Mayor-Council form of government.

*The City needs to carefully consider the many ramifications. One of the most significant, for example, is whether these remediation measures should be enacted to coincide only with the duration of our Mayor-Council governance structure, due to expire in 2010.*

This office has only begun to assess the legal ramifications of these recommendations in this initial and preliminary report. We expect there will be other remediation measures that may also require charter changes.

To avoid inadvertent implementation of the remediation measures in a manner precluded by law, we suggest the Council receive the Mayor's Report but take no immediate action on it as a whole. The Council should consider and ultimately decide which specific measures it wishes to move to implementation. Each such item will be the subject of prompt implementation advice from this office.

Respectfully submitted,



MICHAEL J. AGUIRRE  
City Attorney

MJA:JAK:jk  
RC-2006-25

Attachment

## CITY OF SAN DIEGO

TELEPHONE (619) 236-6220

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Michael J. Aguirre

CITY ATTORNEY

## MEMORANDUM OF LAW

DATE: January 23, 2006

TO: Honorable Mayor and City Councilmembers

FROM: City Attorney

SUBJECT: The Relationship Between the City Offices of the Mayor and the Auditor and Comptroller under the Mayor-Council Form of Government

## QUESTION PRESENTED

What is the relationship between the Office of Auditor and Comptroller [Auditor] of the City of San Diego and the Office of the Mayor under the new Mayor-Council form of government?

## SHORT ANSWER

Under the Mayor-Council form of government implemented January 1, 2006, the Mayor has the express authority to appoint and dismiss the Auditor. That places the office under the Mayor's supervision. However, the Mayor may not limit or impede the authority or duties given to, or required of, this public office by City Charter or ordinance, federal or state law.

## BACKGROUND

On November 2, 2004, the voters of the City of San Diego passed Proposition F, which amended the San Diego City Charter to add Article XV to "test implementation of a new form of governance commonly known as a Strong Mayor form of government." Charter section 250. The five-year trial period of governance is operative January 1, 2006 and continues until December 1, 2010, unless the electorate extends this form of government. Charter § 255. Voters were urged "to elect a chief executive who is accountable for how the City is run, . . . who had the authority to make changes." San Diego Ballot Pamp. General Elec. Nov. 2, 2004, argument in favor of Prop. F.

Voters were told that "the Mayor would have the authority to give direction to all City officers and employees, except those in departments and offices recognized in the Charter as being independent . . . The Mayor would be responsible for preparing the annual budget for the

Council's consideration and adoption. . . . The Mayor would appoint the City Manager with Council confirmation. The City Manager would serve at the pleasure of the Mayor. The Mayor would appoint the City Auditor and Comptroller, Police Chief, and Fire Chief, subject to Council confirmation. All other managerial department heads formerly under the City Manager would be appointed by the Mayor and serve at the pleasure of the Mayor." San Diego Ballot Pamp. General Elec. Nov. 2, 2004, the City Attorney's Impartial Analysis of Prop. F.

Part of the system of "checks and balances" created by Proposition F was the new office of Independent Budget Analyst. San Diego Ballot Pamp. General Elec. Nov. 2, 2004, argument in favor of Prop. F. The City Council would appoint the Independent Budget Analyst: "to review and provide budget information to the Council independent from the Mayor." San Diego Ballot Pamp. General Elec. Nov. 2, 2004, the City Attorney's Impartial Analysis of Prop. F.

Charter section XV was effective January 1, 2006, and with its implementation and the election of a new Mayor, questions have arisen about the relationship between the Office of the Mayor and the Office of the Auditor in the new form of governance.

## DISCUSSION

### I. Charter Changes Impacting the Auditor.

Effective January 1, 2006, the Mayor assumed all executive authority, power, and responsibilities conferred by the Charter upon the City Manager in Article V [Executive and Administrative Service], Article VII [Finance], and Article IX [Retirement of Employees]. Charter § 260 (b). In addition, the Mayor became the Chief Executive Officer of the City of San Diego.<sup>1</sup> Charter § 265 (b) (1).

#### A. The Mayor's Financial Duties.

The Mayor now serves as Chief Administrative and Chief Budget Officer of the City, assuming the duties and responsibilities of the previous City Manager. As such, the Mayor assumed the duties outlined in Charter section 28:

*. . . to supervise the administration of the affairs of the City except as otherwise specifically provided in this Charter; to make such recommendation to the Council concerning the affairs of the City as may seem to him desirable; to keep the Council advised of the financial condition and future needs of the City; to prepare and submit to the Council the annual budget estimate and such reports as*

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<sup>1</sup> The Charter does not define "chief executive officer." But the title commonly means "The highest-ranking executive in a company or organization, responsible for carrying out the policies of the board of directors on a day-to-day basis." *The American Heritage Dictionary of the English Language: Fourth Edition* (2000). (<http://www.bartleby.com/61/90/C0289050.html>)

may be required by that body, including an annual report of all the Departments of the City . . . as Chief Budget Officer of the City, [the Mayor] shall be responsible for planning the activities of the City government and for adjusting such activities to the finances available. To this end he shall *prepare annually a complete financial plan* for the ensuing year and shall be responsible for the administration of such a plan when adopted by the Council. He shall be charged with the *bringing together of estimates covering the financial needs of the City*, with the checking of these estimates against the information relative to past expenditures and income, with the *preparation of the budget document and supporting schedules and with the presentation of the budget to the Council.* (Emphasis added).

In addition, the Mayor is to cooperate fully with the Council and the Office of Independent Budget Analyst, including supplying requesting information concerning the budget process and fiscal condition of the city to the Council and the public. Charter § 265 (b)(14) (15).

**B. Mayor's Supervision of Officers Responsible for Financial Matters.**

With the broad administrative and fiscal responsibilities came the Mayor's authority to appoint and dismiss the City officers responsible for City financial matters. He may appoint and dismiss the City Treasurer as could the previous City Manager. Charter §§ 260 (b), 29, and 45. The amendments to the Charter made no changes in the duties and responsibilities of the office of the Treasurer, which include maintaining custody of and disbursing City moneys, and recording all receipts and expenditures. Charter § 45. Similarly, the Charter transferred the authority to appoint the Auditor from the City Council to the Mayor, subject to Council confirmation, and provides that the Mayor may remove the Auditor subject to appeal to the City Council. Charter §§ 265 (b)(10) and (11). However, the Charter made no changes to the duties of the Auditor. The Auditor remains the "chief fiscal officer of the City" according to Charter section 39, with all of the previously-existing duties and powers.

In assuming the responsibility for the proper administration of all affairs of the City, Charter section 29 gives the Mayor the power to appoint and remove:

. . . all officers and employees in the administrative service of the City under his control; but the [Mayor] may authorize the head of a Department or officer responsible to him to appoint and remove subordinates in such Department or office. Appointments made by, or under the authority of, the [Mayor], shall be on the basis of administrative ability and of the training and experience of such appointees in the work which they are to perform. All such appointments shall be without definite term unless for temporary service not to exceed sixty days. . . Charter § 29.

Under the new form of government, the Office of Auditor and Comptroller was expressly transferred to the new executive branch of City government and the officer holding the position

of Auditor now reports to the highest ranking officer within that branch, the Mayor. However, the Auditor's independent duties, and powers under the City Charter and San Diego Municipal Code have not changed. To help ensure the Auditor's independence, the Charter provides a "checks and balances" by allowing the Auditor to appeal his removal to the City Council. Charter § 265 (b) (11). Nonetheless, the Mayor's responsibilities with respect to the City's finances and budget require that he exercise supervisory authority over the Auditor, subject to other laws that require the Auditor's independence when performing his or her duties.

## II. The Auditor's Authority and Responsibilities Remain Unchanged.

The Office of Auditor is created by the City Charter and the Charter provides the City Council with only limited authority to transfer to others those matters the office might handle that "do not relate directly to the finances of the City." Charter § 39. Accordingly, the Department may not be changed, abolished, combined or rearranged except by a charter change. Similarly, no other Department may be created that would duplicate the duties the charter places upon the Auditor that do relate directly to the finances of the City. *See*, Charter § 26; *Hubbard v. City of San Diego*, 55 Cal.App.3d 380, 387-388 (1976).

In addition, the Mayor would exceed his authority should he impede the performance of the mandatory duties and responsibilities placed upon the Auditor as a public officer by the City Charter, ordinance, or state or federal law. *See, Lockyer v. City and County of San Francisco*, 33 Cal.4th 1055, 1079-1080 (2004). A Mayor in the new form of government only has the authority that is expressly or impliedly conferred upon him or her by a charter. 3 McQuillin, Mun. Corp. (3rd Ed, 2001) § 12.43, p. 266; *see, Bartlett v. Bell*, 58 Cal. App. 357 (1922) [Mayor has no power to compel Auditor to act in matter to benefit a third party].

The duties required of and the power provided to the City Auditor by the City Charter remain intact through the governance change. Charter section 39 specifies the duties of the Auditor and provides, in relevant part, that:

... The City Auditor and Comptroller shall be the chief fiscal officer of the City. He shall exercise supervision over all accounts, and accounts shall be kept showing the financial transactions of all Departments of the City upon forms prescribed by him and approved by the City Manager and the Council. He shall submit to the City Manager and to the Council at least monthly a summary statement of revenues and expenses for the preceding accounting period,<sup>2</sup> detailed as to appropriations and funds in such manner as to show the exact financial condition of the City and of each Department, Division and office thereof. No contract, agreement, or other obligation for the expenditure of public funds shall be entered into by any officer of the City and no such contract shall be valid unless the Auditor and Comptroller shall certify in writing that there has been

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<sup>2</sup> Charter section 89 also requires the Auditor submit similar monthly statements to the Council.

made an appropriation to cover the expenditure and that there remains a sufficient balance to meet the demand thereof.<sup>3</sup> He shall *perform the duties imposed upon City Auditors and Comptrollers by the laws of the State of California, and such other duties as may be imposed upon him by ordinances of the Council*, but nothing shall prevent the Council from transferring to other officers matters in charge of the City Auditor and Comptroller which do not relate directly to the finances of the City. He shall prepare and submit to the City Manager such information as shall be required by the City Manager for the preparation of an annual budget. He shall appoint his subordinates subject to the Civil Service provisions of this Charter. (*Emphasis added*).

Other Charter-mandated duties include the joint determination with the City Attorney of the proper form, arrangement, and itemization of the annual appropriation ordinance; and determination of the "percentage change in price index" (Charter § 71); the keeping of accounts for each item of appropriation; and the transfer of unexpended funds from these accounts to the general fund upon completion of the project or at the end of one year. Charter § 72. If the Council fails to include adequate funds in the appropriation ordinance to cover the Mayor's estimate of the City's debt, or the amount actually required to cover the debt, the Charter requires the Auditor to set up an account for the full amount the Mayor estimates or the amount required to cover the debt, and to transfer tax revenue into that account. Charter § 74. The Auditor has the responsibility to examine all payrolls, bills and other claims against the city (except claims for damages) and has the discretionary authority to investigate such claims (Charter § 82); he is responsible for issuing the checks to pay claims against the City that have been approved by the heads of the Department or offices incurring the debt (Charter § 83); he receives reports from all City officials who collect and deposit money for fees, permits, licenses, inspections, services, taxes, and other municipal charges (Charter §§ 86 and 88); and he determines the appropriate form of accounts to be used by all officers and Departments of the city that receive or disburse City moneys (Charter § 87).

The Auditor must include in his records the cost or value of all City assets; present a balance sheet containing that information to the Mayor-Manager; and publish that information in his annual report. Charter § 112; SDMC § 22.0708. He must audit the accounts of any officer who dies, resigns or is removed from office, and report the results to the Mayor-Manager and Council. If the person is found indebted to the City, the Auditor must notify the Mayor and Council. Charter § 111. And the Auditor has authority to refuse to issue a warrant for a retirement allowance, if, in the Auditor's opinion, the allowance has been granted in contravention of Charter Article IX or ordinances passed under its authority. Charter § 144.

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<sup>3</sup> Charter section 80 also requires the Auditor first certify there are adequate unencumbered funds in the Treasury to cover any contract, agreement, or obligation involving the expenditure of funds before the Council makes such contracts or orders.

The Auditor has additional responsibilities and powers codified in section 7, Article 2 of the San Diego Municipal Code. For example, the Auditor:

... shall, at any time, have power to examine, check and audit the accounts and records of any commission, board, department, division, office, or employee of the City; to require an accounting for all cash revenues of the City; to make and certify to an actual count of cash and securities, and to prescribe, govern and control the movements, or transfer of all cash revenues, or securities, to the custody of the City Treasurer." SDMC §22.0701.

The Mayor and the Auditor must jointly prepare and submit an annual report to the City Council and the Financial Reporting Oversight Board on the status of the City's internal financial controls, with the necessary joint certifications. SDMC § 22.0708. The Auditor also has separate duties associated with the City's Comprehensive Annual Financial Report (CAFR). SDMC §§ 22.0709, 22.0710. Accordingly, the Auditor has many responsibilities and duties outlined in the Charter, City ordinances, and state laws in addition to the reporting obligations to the Mayor and City Council.

### CONCLUSION

Under the new Mayor-Council form of governance, the Auditor reports to the Mayor as Chief Executive Officer of the City of San Diego. Under the Charter, the Auditor is required to support the Mayor in his obligation to provide a budget to the City Council and to provide such other information related to the City's finances and the administration of the City. However, the Auditor does retain some independence in that the Mayor may not limit or impede the authority or duties given to or required of this public officer by Charter, ordinance, federal or state law. Finally, the Auditor's right to appeal his removal to the City Council provides a check and balance on any improper interference with the Auditor's duties and responsibilities.

Respectfully submitted,



MICHAEL J. AGUIRRE  
City Attorney

JK:CMB:jk  
ML-2006-2



OFFICE OF MAYOR JERRY SANDERS  
CITY OF SAN DIEGO

MEMORANDUM

DATE : January 22, 2007  
TO : Council President Peters and Members of the San Diego City Council  
FROM : Mayor Jerry Sanders  
SUBJECT : Establishment of a Charter Review Committee

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In the City's first year operating under Charter Article XV: Strong Mayor Trial Form of Governance it has become apparent there are a number of areas where clarification and fine-tuning would help achieve the original intent of this reform.

In cooperation with the City Attorney's office we have begun to work through some of these issues as they arise, but much more work must be focused on these issues in order to fully prepare for an effective long-term implementation of the Strong Mayor form of governance. I believe we can all agree that when roles and responsibilities are unclear, the business of the public is not optimally served, and that a fresh review of this Charter section is a timely priority.

In addressing these issues, there are four subject areas or questions around which a work plan for the Committee will be set:

- What Charter modifications are necessary to implement the Kroll recommendations and other financial reforms?
- What is a clear definition of the roles and responsibilities of elected officials and the separation of powers under strong mayor?
- What measures may improve the functionality of strong mayor during this trial period?
- What legislative tightening would be required for effective permanent implementation of Article XV?

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Each of these areas will be explored by a designated subcommittee and addressed concurrently in the Committee's work.



Committee meetings will be held twice monthly and will be noticed to the public in keeping with the Ralph M. Brown Act. Subcommittees working in each topic area are anticipated to meet once or twice monthly as is convenient for their membership and in keeping with their work load.

I will move immediately to empanel the Committee in preparation for them to begin their work on or around March 1<sup>st</sup>. It is my intention that the Committee complete its work and return its recommendations in readiness for the 2008 election cycle.

Valuing varied points of view, I would like to work with each of you to identify and nominate three individuals who may be appropriate to serve on the Committee from which I will select one from each of your submissions. In addition, I will make a number of appointments to round out the Committee ensuring a representative balance. We are looking for individuals who can be independent, possess scholarly and operational subject matter expertise, those who have experience with previous charter reform efforts and who are broadly representative of our talented citizenry.

In addition to the Committee members, three ex-officio members will serve as support resources and advisers to the Committee; one each from the City Attorney, Mayor and the Independent Budget Analyst.

I look forward to working with you on these issues so critical to our City's future and welcome your support for this effort.

JS:ACH

City of San Diego  
Disclosure Practices Working Group

Disclosure Controls and Procedures

Article I  
*General*

Section 1.1. Purpose. These Disclosure Controls and Procedures are designed to (i) ensure the accuracy of the City of San Diego's disclosures and the City's compliance (including the City Council, City officers, and staff in the exercise of their official duties) with all applicable federal and state securities laws, and (ii) promote best practices regarding disclosures relating to securities issued by the City and the City's disclosure provided to its Related Entities.

Section 1.2. Disclosure Practices Working Group. Pursuant to Sections 22.4101 and 22.4103 of the Municipal Code, the City Manager, the City Attorney, the City Auditor and Comptroller, and the City Treasurer have established the Disclosure Group.

Section 1.3. Responsibilities of the Disclosure Group. The Disclosure Group shall have the responsibilities set forth in (i) subsection (b) of Section 22.4101 of the Municipal Code, (ii) Section 22.4107 of the Municipal Code, (iii) subsection (a) of Section 22.4109 of the Municipal Code, and (iv) such additional responsibilities as are set forth in these Disclosure Controls and Procedures.

Section 1.4. Rules and Regulations. The Disclosure Group may establish such Rules and Regulations as it determines are appropriate to govern the operation of its meetings and other procedural matters. In the event of any conflict between the terms of the Rules and Regulations and the terms of these Disclosure Controls and Procedures, the terms of the Disclosure Controls and Procedures shall govern.

Article II  
*Definitions*

Section 2.1. Definitions. Capitalized terms used in these Disclosure Controls and Procedures shall have the meanings set forth below:

"CAFR" means the City's Comprehensive Annual Financial Report.

"City" means the City of San Diego, California.

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"*City Financial Statements*" means, individually or collectively as the context may require, CAFR, the audited financial statements of the Metropolitan Wastewater Utility, and the audited financial statements of the Water Utility.

"*Contributors*" means those persons contacted by the Financing Group or the Disclosure Group, or assigned by a department director, to assist with the review or preparation of a Disclosure Document as described in Section 4.3.

"*Deputy City Attorney for Finance and Disclosure*" means the attorney designated as such pursuant to Section 22.0302 of the Municipal Code.

"*Disclosure Documents*" means those documents defined as such in Article III.

"*Disclosure Group*" means the Disclosure Practices Working Group that has been established in the manner described in Section 1.2.

"*Financing Group*" means, collectively, those persons identified as such pursuant to subsection A. of Section 4.3.

"*Municipal Code*" means the San Diego Municipal Code, as amended from time to time.

"*NRMSIRs*" means the nationally recognized municipal securities information repositories approved by the Securities and Exchange Commission to accept the filings referenced in Rule 15c2-12 under the federal Securities Exchange Act of 1934, 17 CFR 240.15c2-12.

"*Preparer*" means those persons defined as such in subsection A. of Section 4.4.

"*Related Entities*" means those entities as defined in Section 22.4102 of the Municipal Code. Related Entities include, but are not limited to, those Related Entities as set forth in Exhibit A, as updated from time to time.

"*Rules and Regulations*" means the rules and regulations established by the Disclosure Group, as described in Section 1.4.

### Article III

#### *Disclosure Documents*

Section 3.1. Disclosure Documents. "Disclosure Documents" means (i) the City's documents and materials prepared, issued, or distributed in connection with the City's disclosure obligations under applicable federal and state securities laws relating to its securities and (ii) any other disclosure which, pursuant to the Municipal Code, the Disclosure Group has the responsibility to review and approve. Disclosure Documents shall include, but not be limited to, the following:

- A. Preliminary and final official statements, and preliminary and final private placement offering documents, relating to the City's securities, together with any supplements;
- B. the City Financial Statements;
- C. any filing made by the City with the NRMSIRs, whether made pursuant to a continuing disclosure agreement to which the City is a party or made voluntarily;
- D. press releases (to the extent that such releases are or could reasonably be construed to be an intended communication to the financial markets), rating agency presentations, postings on the investor information section of the City's webpage, and other communications, reasonably likely, in the determination of the Disclosure Group, to reach investors or the securities markets;
- E. any disclosure materials requiring, pursuant to the Municipal Code, approval and certification by the City Manager, City Attorney, or City Auditor and Comptroller;
- F. disclosures provided by the City in connection with securities issued by Related Entities, together with all of such documents and materials prepared, issued, or distributed in connection with such securities, to the extent that the City, the City Council, or City officers, or staff are responsible for the form or content of such documents or materials;
- G. offering documents prepared by Related Entities if such documents are subject to the approval of the City Council; and
- H. such portions of the City's published adopted annual budget as the Disclosure Group determines to be appropriate, which shall at a minimum include the executive summary.

#### Article IV *Review Process*

Section 4.1. Determination of "Disclosure Document" status. Whether a particular document or written, posted or other communication is a Disclosure Document shall be determined by the Disclosure Group, including the determination whether a document should be filed voluntarily with the NRMSIRs (see Section 3.1.C.) or whether a communication is reasonably likely to reach investors or the securities markets (see Section 3.1.D.). To assist the Disclosure Group in its determination whether a particular document is a Disclosure Document as described in subsection F. of Section 3.1,

information shall be solicited from the appropriate Related Entity by means of a letter in the form attached as Exhibit B.

Section 4.2. Review of Form and Content of Disclosure Documents. The Disclosure Group shall review the form and content of each Disclosure Document.

Section 4.3. Review of Official Statements. The following procedures shall apply to those Disclosure Documents described in subsections A. or G. of Section 3.1:

A. Financing Group. Financial Services shall timely identify for the Disclosure Group a Financing Group for each financing (the composition of which may differ for each financing), which shall include the Deputy City Attorney for Finance and Disclosure (or such other Deputy City Attorney designated to work on the matter by the Deputy City Attorney for Finance and Disclosure), such manager of Financing Services as the City Treasurer determines to be the appropriate interface with the bond financing team (i.e., bond counsel and/or disclosure counsel, underwriter(s), underwriter's counsel, financial advisors, and appropriate City staff), the City's outside disclosure counsel, and such other members of the Disclosure Group as the Disclosure Group determines to be appropriate.

B. Responsibilities of Financing Group. The Financing Group shall (i) assist the bond financing team in the preparation of the Disclosure Document and (ii) the manager of Financing Services working with the Financing Group shall certify to the Disclosure Group that, to the best of his/her knowledge, these Disclosure Controls and Procedures were followed in such preparation.

1. The Financing Group shall be responsible for soliciting material information from City departments. The Financing Group shall identify Contributors who may have information necessary to prepare or who should review portions of the Disclosure Document. These Contributors should be timely contacted and informed that their assistance will be needed for the preparation of the Disclosure Document, which notification will contain the information set forth in Exhibit C.

2. The Financing Group shall contact the individuals and departments identified as Contributors as soon as possible in order to provide adequate time for such individuals to perform a thoughtful and thorough review or draft of those portions of the Disclosure Document assigned to them.

3. The manager of Financing Services assigned to the financing, together with the Deputy City Attorney for Finance and Disclosure, shall maintain or cause to be maintained an accurate log of all individuals or departments that were requested to review or draft information in connection with a Disclosure Document, including what sections such individuals or department prepared or reviewed. The Deputy City Attorney for Finance and Disclosure shall also be responsible for collecting all transmittal letters, certifications, and lists of sources for incorporation into the minutes maintained by the Disclosure Group.

4. The Financing Group shall confirm to and advise the Disclosure Group that each section of and all financial and operating information contained in the Disclosure Document has been reviewed by an appropriate person, as evidenced by the written material described in 3. above (which shall constitute the "audit trail" referenced in Section 22.4105(a)(4) of the Municipal Code). Of particular import is that the "Appendix A" and other information concerning the City is thoroughly compared for accuracy against the City Financial Statements. The Financing Group shall review the letters and any accompanying information provided pursuant to subsections C. through G. of this Section 4.3 and shall transmit such materials to the Disclosure Group, such letters to be substantially in the form set forth in Exhibit D.

5. The Financing Group shall report any significant disclosure issues and concerns to the Disclosure Group as they are discovered.

6. The Financing Group shall advise the financial advisor and the underwriter(s) and their counsel, that they must execute upon their selection a confidentiality agreement substantially in the form attached as Exhibit E.

C. Responsibilities of Contributors. A Contributor shall assist in reviewing and preparing the Disclosure Document using his or her knowledge of the City and by discussing the Disclosure Document with other members of the department in an attempt to ensure the accuracy of the information and to determine whether any other information should be discussed or disclosed. Once a Contributor is notified of his or her need to participate in preparing a Disclosure Document, the Contributor and the Contributor's department director shall cooperate with Financing Group and Disclosure Group requests.

D. Review by Human Resources Manager. With respect to those Disclosure Documents described in subsection A. of Section 3.1 that relate to securities that are secured directly or indirectly by the City's general fund, the Financing Group shall forward the Disclosure Document to the Human Resources Manager for review by means of a letter substantially similar to Exhibit C. In particular, the Human Resources Manager and the Personnel Director shall review any information in the Disclosure Document relating to employee relations, collective bargaining, pensions and benefits, and litigation concerning current or former employees. The Human Resources Manager shall timely send any comments on the Disclosure Document to the Financing Group after receiving the Disclosure Document, by means of the transmittal letter attached as Exhibit F.

E. Review by San Diego City Employees' Retirement System (SDCERS). With respect to those Disclosure Documents described in subsection A. of Section 3.1 that relate to securities that are secured directly or indirectly by the City's general fund, the Financing Group shall forward the Disclosure Document to the [Retirement Administrator, Head of the Investment Division, Head of the Administration Division and Head of the Legal Division] by means of a letter substantially similar to Exhibit C. Such individuals shall be requested to review any information in the Disclosure

Document relating to pension benefits and other retirement benefits, pension plan funding and litigation concerning SDCERS. Any comments on the Disclosure Document shall timely be sent to the Financing Group after receiving the Disclosure Document, by means of the transmittal letter attached as Exhibit G.

F. Review by City Attorney for Litigation. The Deputy City Attorney for Finance and Disclosure shall transmit the Disclosure Document to the appropriate attorneys in the City Attorney's office who are responsible for identifying any material current, pending or threatened litigation. The responsible attorneys shall timely draft descriptions of any such litigation, and of any material settlements or court orders, for the Disclosure Document after receiving the Disclosure Document. The responsible attorneys shall timely transmit the requested information to the Financing Group after receiving the Disclosure Document, by means of the transmittal letter attached as Exhibit H.

G. Review by City Auditor and Comptroller. The Financing Group shall forward the Disclosure Document to the City Auditor and Comptroller by means of a letter substantially similar to Exhibit C. The City Auditor and Comptroller shall designate one or more employees to assist the Financing Group with comparing and noting any discrepancies between the City Financial Statements and the Disclosure Document. The City Auditor and Comptroller shall also review the Disclosure Document in full to identify any material difference in presentation of financial material from the Financial Statements, any misstatement or omission in any sections that contain descriptions of information prepared by or of interest to the City Auditor and Comptroller. Any comments on the Disclosure Document shall timely be sent to the Financing Group after receiving the Disclosure Document, by means of the transmittal letter attached as Exhibit I.

H. Reference Materials. The Deputy City Attorney for Finance and Disclosure and the City's outside disclosure counsel, in providing advice to the Disclosure Group regarding the contents of those Disclosure Documents described in subsections A. or G. of Section 3.1, shall review and take into consideration the reference materials listed in Exhibit J, as updated from time to time.

Section 4.4. Review of Disclosure Documents other than Official Statements. The following procedures shall apply to those Disclosure Documents that are not addressed in Section 4.3:

A. Determination of Disclosure Document. Any person (each, a "Preparer") preparing any information for release to the public that could be considered a Disclosure Document and that is not otherwise identified as a Disclosure Document in the forward calendar referenced in Section 6.3, shall notify the Disclosure Group of such information. The Disclosure Group shall timely make a determination whether such information is a Disclosure Document pursuant to Section 4.1.

B. Notify Disclosure Group. If it is determined that a document is a Disclosure Document, the Preparer shall inform the Disclosure Group of the (i) expected

completion date of the Disclosure Document and (ii) the expected or required dissemination date of the Disclosure Document.

C. Involvement of Deputy City Attorney. The Deputy City Attorney for Finance and Disclosure, in consultation with the City's outside disclosure counsel, shall assist the Preparer to:

1. identify material information that should be disclosed;
2. identify other persons that may have material information or knowledge of any information omitted from such Disclosure Document; and
3. determine when the Disclosure Document is final and ready for review by the Disclosure Group.

D. Prepare Source List. The Preparer shall keep a list of individuals or groups that have contributed to the preparation of the Disclosure Document and a list of sources from which the information summarized or updated in the Disclosure Document was derived. These lists shall be submitted to the Disclosure Group along with the Disclosure Document.

## Article V *Approval Process*

Section 5.1. General. The Disclosure Group shall review and approve the form and content of each Disclosure Document. Such approval shall be evidenced by the affirmative vote of a majority of a quorum of the Disclosure Group, as determined by the Rules and Regulations. The Disclosure Group may determine that those Disclosure Documents that (i) the City is contractually obligated to file with the NRMSIRs if determined to be a material event or as a result of the failure to file the required annual financial information and (ii) contain no discretionary content (e.g., rating changes), may be filed with the NRMSIRs upon the approval of the City's outside disclosure counsel and at least one other member of the Disclosure Group.

Section 5.2. Submission of Official Statements to Disclosure Group for Approval. The Financing Group shall submit any Disclosure Document described in Section 4.3 to the Disclosure Group when (i) it has obtained all of the approvals and source documentation described in Section 4.3, and (ii) in its best judgment, the Disclosure Document is in substantially final form. Such submission shall be by means of the transmittal letter attached as Exhibit K.

The Disclosure Group shall critically evaluate the Disclosure Document for accuracy, and have the opportunity to ask questions of the Financing Group and of any Contributor or other person who reviewed or drafted any section of the Disclosure Document. The Disclosure Group may send the Disclosure Document back to the Financing Group for revisions. The Disclosure Group shall timely contact the Financing



Group with any comments or questions on the Disclosure Document or the associated financing.

Section 5.3. Submission of Official Statements to City Manager and City Attorney. The Disclosure Group shall submit any Disclosure Document described in Section 4.3 to the City Manager and City Attorney when, in its best judgment, (i) the Disclosure Document is in substantially final form and (ii) the Disclosure Group has complied with these Disclosure Controls and Procedures. Such submission shall be by means of the transmittal letter attached as Exhibit L.

The City Manager and City Attorney shall critically evaluate, or cause to be evaluated, the Disclosure Document for accuracy. The City Manager and the City Attorney shall meet with the Financing Group and the Disclosure Group at a mutually convenient time, and ask questions of the Financing Group, the Disclosure Group, any Contributor, and any other person who reviewed or drafted any section of the Disclosure Document. The City Manager or City Attorney may send the Disclosure Document back to the Financing Group for revisions. Upon satisfaction with the Disclosure Document, the City Manager and City Attorney shall execute the certifications required by Section 22.4111(a) of the Municipal Code, in the form attached as Exhibit M, and provide a copy to the Disclosure Group.

Section 5.4. City Auditor and Comptroller Certification. Upon satisfaction with a Disclosure Document described in Section 4.3 or in subsection F. of Section 3.1, the City Auditor and Comptroller shall execute the certification required by 22.0709(b) of the Municipal Code, in the form attached as Exhibit N, and provide a copy to the Disclosure Group. With respect to each CAFR, the City Auditor and Comptroller shall execute the certification required by 22.0709(a) of the Municipal Code, in the form attached as Exhibit O, and provide a copy to the Disclosure Group.

Section 5.5. Submission of Official Statements to City Council for Approval. As part of the docketing process, the Disclosure Group shall submit any Disclosure Document described in Section 4.3 to the City Council for approval together with the certifications from the City Manager, the City Attorney, and the City Auditor and Comptroller promptly after the receipt of such certifications. The approval of such a Disclosure Document by the City Council shall be docketed on the adoption agenda and not be approved as a consent item. The City Council shall undertake such review as they are advised by the Deputy City Attorney advisor to the City Council appointed pursuant to Section 22.0303 of the Municipal Code and the City's outside disclosure counsel to be appropriate to fulfill their responsibilities under applicable federal and state securities laws.

Section 5.6. Approval of Disclosure Documents other than Official Statements. Any Disclosure Document and accompanying source lists described in Section 4.4 shall be submitted to the Disclosure Group for approval when the Preparer, the Deputy City Attorney for Finance and Disclosure, and the City's outside disclosure counsel believe such Disclosure Document is ready for dissemination.

The Disclosure Group shall critically evaluate the Disclosure Document for accuracy and sufficiency, and have the opportunity to ask questions of the Preparer or any other person who reviewed or drafted any section of the Disclosure Document. The Disclosure Group may send the Disclosure Document back to the Preparer for revisions. The Disclosure Group shall contact the Preparer with any comments or questions on the Disclosure Document or the associated financing by no later than (a) in the case of a Disclosure Document scheduled on the forward calendar referenced in Section 6.3., the later of (i) five (5) business days after receiving such Disclosure Document and (ii) the business day immediately succeeding the next regularly scheduled meeting of the Disclosure Group, or (b) in the case of an unscheduled Disclosure Document, as soon as reasonably practicable.

## Article VI

### *Timelines for Review*

Section 6.1. Timelines for Review of Official Statements. The timeline for any particular bond financing for which a Disclosure Document as described in subsections A. or G. of Section 3.1 will be used will vary depending on the type of bonds being offered (e.g., variable rate, fixed rate, auction rate), the security for the bonds (e.g., general obligation, revenue pledge), the purpose for the financing, and other factors unique to each bond financing. Accordingly, the following timeline has been developed to assist the Disclosure Group, each Financing Group, and each bond financing team in developing a bond financing schedule, but is intended only to provide very general guidance in light of the unique characteristics of each bond financing.

Day 270	Disclosure Group notified of the bond financing by inclusion of the financing on the forward calendar referenced in Section 6.3, and identifies a Financing Group
Days 150-270	Financing Group meets with the bond financing team to understand basics of bond financing; initial draft of Disclosure Document is prepared
Day 150	Financing Group distributes information to Contributors and department directors
Day 150	Financing Group distributes information to Human Resources Manager, SDCERS representative, and City Auditor and Comptroller, as may be applicable
Day 130	Deputy City Attorney for Finance and Disclosure transmits Disclosure Document to appropriate litigation attorneys in City Attorney's Office
Days 110-130	Department directors and Contributors discuss Disclosure Document at departmental meetings

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Day 100	Contributors submit requested information to Financing Group
Day 90	Human Resources Manager, SDCERS representative and City Attorney representative transmit any requested information to Financing Group
Days 60-90	Financing Group reviews Disclosure Document and all related materials, and transmits to Disclosure Group
Days 40-60	Disclosure Group reviews Disclosure Document and all related materials, and submits to City Manager and City Attorney
Days 30-40	City Manager and City Attorney meet with Disclosure Group
Day 30	City Manager and City Attorney execute required certifications
Day 29	Disclosure Group submits Disclosure Document and related certifications to City Council as part of the docketing process referenced in Section 5.5
Day 15-29	City Council briefed regarding Disclosure Document by Deputy City Attorney advisor to the City Council and the City's outside disclosure counsel
Day 5	City Council approves Disclosure Document
Day 0	Preliminary Official Statement is mailed
Day 0 – Delivery Date (or such later date through which the City is contractually obligated to advise the bond financing team of material events)	Financing Group advises Disclosure Group of (i) any material changes to Preliminary Official Statement to create the final Official Statement and (ii) any material changes to the final Official Statement up to and including the date of delivery of the bonds. In either such event, the Disclosure Group must review and approve the form and content of the material change disclosure and determine whether it is necessary or appropriate to submit the material change disclosure to the City Council for approval.

Section 6.2. Timelines for Review of Disclosure Documents other than Official Statements. The timeline for preparing any particular Disclosure Document will vary depending on the type of Disclosure Document and whether or not the Disclosure Document was on the forward calendar referenced in Section 6.3. Accordingly, the following timeline has been developed to assist the Disclosure Group and the Preparer in developing a schedule, but is intended only to provide very general guidance in light of the unique characteristics of each Disclosure Document.

Action	Scheduled (measured by days before Disclosure Document dissemination scheduled)	Unscheduled (measured from days after unexpected Disclosure Document revealed)
Disclosure Group notified of the potential Disclosure Document	60 days	ASAP
Disclosure Group makes a determination whether a document is a Disclosure Document	N/A	2 business days
Preparer, Deputy City Attorney for Finance and Disclosure, and the City's outside disclosure counsel identify other persons that may have material information or knowledge of any information omitted from such Disclosure Document	50-60 days	4 business days
Disclosure Document finalized and transmitted to Disclosure Group	25-50 days	4-5 business days
Disclosure Group reviews Disclosure Document and all related materials, and approves Disclosure Document for dissemination	10 days	5-6 business days

Section 6.3. Forward Calendar. The Disclosure Group shall develop a forward calendar that sets forth, to the best judgment of the Disclosure Group, a comprehensive list of Disclosure Documents that are subject to the review and approval of the Disclosure Group over the next twelve months. Such forward calendar shall be revised from time to time, and every effort shall be made to keep such document current. The City Treasurer shall advise the Disclosure Group of all Disclosure Documents originating in Financing Services (being those Disclosure Documents described in subsection A. of Section 3.1, and those Disclosure Documents filed by the City with the NRMSIRs pursuant to continuing disclosure agreements described in subsection C. of Section 3.1) that are expected to be submitted to the Disclosure Group for review and approval over the next twelve months. In addition, the City Treasurer shall advise the Disclosure Group, after soliciting the appropriate information from the Related Entities, of those Disclosure Documents described in subsections F. or G. of Section 3.1 that are expected to be submitted to the Disclosure Group for review and approval over the next twelve months. The City Auditor and Comptroller shall advise the Disclosure Group of the dates that the CAFR, the audited financial statements of the Metropolitan Wastewater Utility, the audited financial statements of the Water Utility, the Disclosure Documents described in subsection B. of Section 3.1, and any other Disclosure Document, are expected to be

submitted to the Disclosure Group for review and approval over the next twelve months. The Deputy City Manager for Finance shall advise the Disclosure Group of the date that the Disclosure Document described in subsection H. of Section 3.1 is expected to be submitted to the Disclosure Group for review and approval over the next twelve months.

## Article VII *Training Policy*

### Section 7.1. Training Sessions.

A. Employees with responsibility for collecting or analyzing information that may be material to the preparation of a Disclosure Document shall attend disclosure training sessions conducted by the City's outside disclosure counsel, with the assistance of the Deputy City Attorney for Finance and Disclosure appointed pursuant to Section 22.0302 of the Municipal Code. New employees shall attend such a session within three months of their first day of employment. Such training sessions shall include education on the City's disclosure obligations under applicable federal and state securities laws and their responsibilities and potential liabilities regarding such obligations, the anonymous and confidential contact information for the Financial Reporting Oversight Board described in Section 9.2, and the contact information for the Deputy City Attorney for Finance and Disclosure. Such training sessions may be conducted by videotape.

B. The determination as to whether or not an employee shall receive such training shall be made by the Deputy City Manager, the City Auditor and Comptroller, or the City Attorney, as appropriate, responsible for such employee. The Disclosure Group may also require training for an employee not specified by any such person.

C. Separate training sessions shall be conducted by the City's outside disclosure counsel, with the assistance of the Deputy City Attorney for Finance and Disclosure and the Deputy City Attorney designated as an advisor to the City Council pursuant to Section 22.0303 of the Municipal Code, for the Mayor and City Council members.

## Article VIII *Document Retention Policies*

### Section 8.1. Official Statements.

A. Materials retained. The Disclosure Group shall retain in a central depository, for a period of five years from the date of delivery of the securities referenced in a Disclosure Document described in subsections A. or G. of Section 3.1, the following materials:

1. the printed copy of the Preliminary and final Official Statement (or Preliminary and final Offering Memoranda);
2. the "deemed final" certification provided by a City official to the underwriter of the securities in accordance with paragraph (b)(1) of Rule 15c2-12;

3. the executed copies of the letters, requests, and certifications, the forms of which are attached as Exhibits B-K, and M;

4. the information and related sources referenced in the materials described in 3. above;

5. the bond purchase agreement; and

6. any written certification or opinions executed by a City official relating to disclosure matters, delivered at the time of delivery of the related securities.

B. Materials not retained. The Disclosure Group shall not retain after the date of delivery of the related securities the drafts of any of the materials referenced in subsection A. above.

Section 8.2. Disclosure Documents other than Official Statements. The Disclosure Group shall retain in a central depository, for a period of five years from the date the respective Disclosure Document is published, posted, or otherwise made publicly available:

1. the final version of the Disclosure Document,

2. all transmittal letters, requests, and certifications relating to information in the Disclosure Document,

3. the information and related sources referenced in the materials described in 2. above.

The Disclosure Group shall not retain the drafts of any such materials.

## Article IX

### *Confidential Submissions*

Section 9.1. Deputy City Attorney for Finance and Disclosure. The City shall encourage City employees to contact the Deputy City Attorney for Finance and Disclosure with any disclosure questions or concerns. To the extent permitted by law, upon the employee's request, the Deputy City Attorney for Finance and Disclosure shall keep the employee's identity confidential.

Section 9.2. Financial Reporting Oversight Board (FROB) Contact Information. The City shall set up a confidential and anonymous system so that City employees can contact the FROB with any concerns about accounting or financial disclosure issues if they prefer not to contact the Deputy City Attorney for Finance and Disclosure. The FROB will create a procedure for contacting them in an anonymous and confidential manner.

Article X  
*Annual Review*

Section 10.1. Annual Review. The Disclosure Group shall conduct an annual evaluation of these Disclosure Controls and Procedures and prepare an annual report, in accordance with the procedures and the dates established by Section 22.4106 of the Municipal Code.

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### Exhibits

- A. List of Related Entities
  - B. Related Entity Letter
  - C. Request for Information from Contributors
  - D. Transmittal by Department Director or Deputy City Manger to Financing Group
  - E. Underwriter's/Financial Advisor's Confidentiality Agreement
  - F. Letter from Human Resources Manager
  - G. Letter from SDCERS Representative
  - H. Letter from City Attorney's Office Regarding Litigation
  - I. Letter from City Auditor and Comptroller
  - J. Municipal Finance Disclosure Reference Materials
  - K. Transmittal of Official Statement by Financing Group to Disclosure Group
  - L. Transmittal of Official Statement by Disclosure Group to City Manager and City Attorney
  - M. Certifications by City Attorney and City Manager
  - N. Certification by City Auditor and Comptroller Regarding Official Statements
  - O. Certification by City Auditor and Comptroller Regarding CAFR
-